United States Court of Appeals

for the Second Circuit

APPELLEE’S BRIEF

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United States Court of Appeals
For the Second Circuit

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HARVEY R. MILLER, as Trustee in Bankruptcy of IRA HAUPT & CO., a Limited Partnership, Bankrupt,
Plaintiff-Appellant,

PJS

against

NEW YORK PRODUCE EXCHANGE, *et al.*,
Defendants-Appellees.

Appeal from a Judgment of the United States District Court for the Southern District of New York

BRIEF OF DEFENDANTS-APPELLEES

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3

TABLE OF CONTENTS

PAGE

I. Cases:

II. Statutes, Rules and Regulations:

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Preliminary Statement

Plaintiff brings this lawsuit on behalf of one of the leading wrongdoers in the 1963 Salad Oil Swindle, Ira Haupt & Co. ("Haupt"). The claim is that defendant New York Produce Exchange (the "Exchange") and its directors failed in their duty to prevent unlawful acts in which Haupt itself was a knowing and willing participant.

Plaintiff conducted massive discovery for seven years, in an unsuccessful search for evidence of wrongdoing by someone other than Haupt and its customer, Anthony De-Angelis. Thereafter, defendants moved for summary judgment. The District Court, giving plaintiff the broadest possible latitude, denied the motions. Despite—or perhaps because of—the complexity of the facts and the esoteric nature of the transactions involved, plaintiff then insisted on trying his case to a jury.

Plaintiff's case took nearly six weeks to present, six weeks in which plaintiff sought to put before the jury improper and inflammatory materials as a substitute for evidence of wrongdoing. On some occasions (as with a work of journalism on the Salad Oil Swindle) the court rejected the purported "evidence"; on others (as with misleading charts) the court felt compelled to give the plaintiff leeway. At the close of plaintiff's case, the court dismissed the allegations of bad faith for failure of proof and reserved on the motion to dismiss the entire complaint (JA 1794a).*

Defendants put in their case in approximately two trial days. They demonstrated, beyond all possible doubt, that Haupt had been guilty of willful misconduct which caused its own losses. After plaintiff's rebuttal case, the trial court, while doubtful that the jury could find for plaintiff (JA 2094a), again deferred decision on defendants' motions for a directed verdict and sent the case to the jury. At the end of seven weeks of trial, the jury returned a verdict for the defendants.

* "JA" refers to the Joint Appendix. Plaintiff's exhibits are designated "PX" and defendants' "DX", followed by the Joint Appendix reference. "Br." refers to plaintiff's brief in this Court.

Plaintiff now seeks to have this Court overturn the jury's verdict, so that he can try his luck again for another seven weeks before another jury, 13 years or more after the events in suit.

We respectfully submit that plaintiff has had his day in court, and indeed many more days than he is entitled to. The case should never have gone to trial; it should never have gone to the jury; and certainly there was no error below of which plaintiff can complain. The judgment entered on the jury verdict should be affirmed.

Issues Presented

1. In an action brought under the Commodity Exchange Act and the antitrust laws against a commodity exchange and its directors, on behalf of a registered futures broker, judgment for defendants was required as a matter of law, because:

(a) the broker on whose behalf the action was brought was indisputably guilty of more culpable conduct than any act of which defendants are accused;

(b) even apart from the broker's misconduct, the Commodity Exchange Act creates no private right of action on the facts of this case;

(c) assuming the existence of a private right of action, defendants did not violate the applicable standards of conduct; and

(d) no act or omission of any defendant was a proximate cause of the injury sued for.

2. The District Court did not err in those portions of its charge to the jury of which plaintiff complains.

3. The District Court did not err in excluding evidence offered by plaintiff or in admitting into evidence an official report of a United States government agency.

Statement of the Case

An accurate statement of the case demonstrates that while Haupt was engaged in willful wrongdoing, defendants regulated the cottonseed oil futures market honestly and diligently, and even almost rescued Haupt from the consequences of its own misconduct. Indeed, as a Haupt partner said at the time, defendants "upheld every good tradition of Wall Street and the investment community." (DX 106, JA 1111e).

The Parties

(a) Plaintiff and Haupt

Plaintiff understandably prefers the cloak of "the Trustee,"* but it is clear that Haupt is the real plaintiff in this case. It was not disputed below, and it is not disputed on this appeal, that plaintiff stands in Haupt's shoes, and can have no greater rights than Haupt would have if it were the named plaintiff. 4A Collier *Bankruptcy* §70.28, p. 385 (14th ed. 1971); *Seligson* v. *New York Produce Exchange,* 378 F. Supp. 1076, 1085-86 (S.D.N.Y. 1974).

* Upon the death of the original plaintiff, Charles Seligson, Harvey R. Miller succeeded as trustee in bankruptcy and as plaintiff. "Plaintiff" refers to either or both of the trustees, as the context requires.

Haupt was, in 1963, an old-line New York Stock Exchange firm. It had also been a member of the New York Produce Exchange for more than twenty years. It was a member of the American Stock Exchange, several other stock and commodity exchanges, and a futures commission merchant (*i.e.,* broker) registered with the Secretary of Agriculture. Haupt was totally respectable in the eyes of the outside world, including the defendants (*e.g.,* Boyer, JA 463a; Weinstein, JA 484a-485a; Berg, JA 756a; Fashena, JA 979a-981a). Out of greed for commissions, however, it became intimately involved with the perpetrator of the Salad Oil Swindle, Anthony DeAngelis, and his corporate vehicles, principally Allied Crude Vegetable Oil Refining Corporation (collectively referred to as "Allied").

Haupt accumulated, on Allied's behalf, a huge long position in the cottonseed oil futures market. As broker for Allied, Haupt was the buyer on more than 80% of all the cottonseed oil futures contracts that were in existence in mid-November 1963 (DX 214, JA 1275e-1277e). Incredibly, plaintiff's claim here is that *defendants* should have detected and halted Haupt's own huge accumulation of contracts sooner than they did.

(b) Defendants

Defendants include the Exchange, on which cottonseed oil futures contracts were traded in 1963, and five members of its 15-man Board: Donald V. MacDonald, Harry B. Anderson, Walter C. Klein, Harold H. Vogel and Sidney Fashena. These five men constituted the Executive Committee of the Exchange; in addition, MacDonald held the office of President, Vogel was Vice President, and Fashena

was Treasurer. The Exchange was a nonprofit corporation, and all the individual defendants—indeed all directors of the Exchange—worked full time in other occupations and served the Exchange without compensation.

The Exchange was a small organization, with 400 members and about 20 employees, only one of whom, the Managing Director, Carl R. Berg,* had executive status. Having just marked its one hundredth anniversary, in 1963 the Exchange was effectively wrecked by the events involved in this litigation.

Neither Allied nor DeAngelis was at any time a member of the Exchange.

Also named as defendants are Merrill Lynch, Pierce, Fenner & Smith Incorporated ("Merrill Lynch"), Bunge Corporation ("Bunge") and Continental Grain Company ("Continental"), the employers of Anderson, Klein and Vogel, respectively, and I. Usiskin & Co. ("Usiskin"), a two-man partnership (defunct since 1967) of which Fashena was a member. Merrill Lynch, Bunge, Continental and Usiskin were sued solely on a theory of vicarious liability, and the complaint was dismissed against them at the close of plaintiff's case.

In an effort to obscure the indisputable evidence adduced at trial, plaintiff labels all the individual defendants as "trader-regulators." He suggests that they all had "the inherent conflict of wearing two hats" (Br., p. 2),

* Berg was originally named as a defendant. He died in 1971, and the complaint against him was dismissed for failure to make a timely motion to substitute his executor. Berg had been a full-time salaried executive of the Exchange since 1947.

by regulating the cottonseed oil market and trading in it. This is false:

—MacDonald never traded a pound of cottonseed oil for himself (McDonald, JA 628a). He was a salaried employee of Fahnestock & Co.,* a firm which in 1963 did no trading in cottonseed oil futures for itself and very little for customers (McDonald, JA 628a).

—Anderson, the head of Merrill Lynch's commodity department, was an administrator, not a trader (Anderson, JA 1174a). Anderson never owned any cottonseed oil futures contracts. Merrill Lynch itself acted strictly as broker, executing orders in cottonseed oil futures exclusively for customers and had no proprietary interest in the market (Dahl, JA 386a-388a; Anderson, JA 1174a).

—Klein represented the grain trade, not the vegetable oil trade, on the Exchange Board of Managers (Klein, JA 1375a-1377a, 1425a), and as President of Bunge was primarily concerned with Bunge's grain business, not its oil business. Klein was not a trader of any commodity futures (Klein, JA 1417a).

—Vogel also represented the grain trade on the Board of Managers (Vogel, JA 1510a); his employment as Executive Vice President of Continental was exclusively concerned with the grain business, and had nothing to do with any vegetable oil (Vogel, JA 1501a-1504a). Indeed, Continental entered the vegetable oil business, through merger

* Fahnestock & Co. was originally named as a defendant, but was granted summary judgment on May 17, 1974. This decision has not been appealed.

with an affiliated company, only in March 1963, after Vogel had been on the Exchange Board for several years (Vogel, JA 1501a, 1507a).

—Fashena, a floor broker, was the only cottonseed oil trader among the individual defendants. But Fashena did no cottonseed oil trading at all in the critical period in issue; his own position and that of his firm were insignificant, and the long and short contracts they held just about balanced each other out. Fashena was, as the court below found, a peripheral figure in the events here challenged, "not someone to whom others turned for advice or with whom others felt obliged to touch base on matters of import." *Seligson* v. *New York Produce Exchange*, 378 F. Supp. 1075, 1104 (S.D.N.Y. 1974).

The Exchange by-laws required that nominees for the Board of Managers be fairly apportioned among the different trade interests of the Exchange (PX 55, §7, JA 259e). However, individuals were elected to the Board by the entire membership and served on the Board in their personal capacities, not as representatives of their firms, just as directors of a bar association represent the membership and not their own law firms.

The Futures Markets

Plaintiff has chosen to omit several key aspects of futures trading from the exposition in his brief.

The Obligations of Exchange Members. Plaintiff, while taking a broad view of the Exchange's regulatory duties (Br., pp. 28-30), nowhere mentions the fact that Exchange

members—like Haupt—had duties of their own. All Exchange members, including Haupt, undertook as a condition precedent to membership on the Exchange "to abide and be bound by and subject to all of the provisions of [the] Charter, By-laws, Rules and Regulations" of the Exchange* (DX 7, JA 1037e-1090e; MacDonald, JA 630a; Berg, JA 835a-841a). Among the duties imposed by the written Exchange By-laws, Rules and Regulations was the duty not to engage in manipulative activity (PX 55, §68, JA 259e; PX 56, Rule 5, JA 303e; see also, Commodity Exchange Act §9, 7 U.S.C. §13); not to engage in improper ex-pit transactions (PX 55, §66, JA 259e; PX 56, Rule 6, JA 303e); to obtain adequate margins from their customers (PX 56, Rule 31, JA 303e); and to make accurate reports of transactions (PX 56, Rule 15, JA 303e; Commodity Exchange Act §§4b, 4c, 7 U.S.C. §§6b, 6c). It is implicit in plaintiff's theory of the case that Haupt violated every one of these rules.

In addition, Haupt was bound by the "know-your-customer" rule, the very cornerstone of self-regulatory exchanges (Leuthold, JA 231a; Dahl, JA 315a; MacDonald, JA 524a; DX 209, JA 1193e-1195e**). It is self-evident in this case that Haupt glaringly violated the know-your-customer rule.

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* Only individuals were members of the Exchange. However, through the membership of the individuals, their firms could become registered members, pursuant to Section 69 of the by-laws (PX 55, §69, JA 259e). Registered members had the same duties to the Exchange as individual members.

** As one of plaintiff's experts, Dr. Gray, wrote: "The know your customer rule . . . in the final analysis must be relied upon to protect legitimate commerce, no matter how many procedural rules are specified." (DX 209, JA 1193e-1195e).

The Confidentiality of Traders' Positions. The positions of traders on the Exchange were closely guarded secrets; neither the traders nor the Exchange members told the Exchange how many contracts they held. This information was reported in code by the traders, and also by Exchange members who carried positions for customers, directly to the Commodity Exchange Authority ("CEA") (Ellison, JA 255a; Dahl, JA 287a-289a, 306a; McMinn, JA 872a, 885a-886a.) By law, this information was declared confidential and with limited exception could not be released. (Commodity Exchange Act, 7 U.S.C. §8; Ellison, JA 243a, 256a, 259a.) Because of this, the Exchange necessarily relied upon its members as a first line of defense against unlawful conduct by the members' customers.

DeAngelis, who testified as plaintiff's witness, confirmed that his position was a closely guarded secret (JA 1099a-1102a). Another plaintiff's witness, John Fontana, who traded for Allied on the Exchange floor, testified that although he was regarded by DeAngelis as a member of his family, he did not know Allied's position (JA 442a-453a). Thus, while the CEA and Haupt knew at every moment exactly how many contracts Haupt held for Allied, it is undisputed that no defendant knew how many contracts Allied held until November 14, 1963—when Allied's position, held almost entirely by Haupt, had reached 90% of the total.

The Role of the New York Produce Exchange Clearing Association ("Clearing Association"). All contracts traded on the Exchange were cleared through the Clearing Association, a stock corporation which was distinct from and independent of the Exchange. The Clearing Associa-

tion became the opposite party on every contract it cleared, guaranteeing that each such transaction would be honored (JA 460a-461a). Gain or loss on contracts and consequent margin payments were calculated by the Association daily, with the Association itself always in a zero position at the close of the day (Boyer, JA 462a).*

If there was an upward variation in the price of the contracts, clearing members carrying long positions received payments of variation margin from the Association and clearing members carrying short positions paid variation margin to the Association; conversely, a downturn in price would result in variation margin payments by the longs to the Association, and by the Association to the shorts. The carrying members then credited or required payment from their own customers.

Between September 1 and November 13, 1973, when the price of cottonseed oil futures contracts went up, Haupt on behalf of its customer Allied received payments totaling $10,840,000 in variation margin from the Clearing Association (DX 146, 1119e-1138e). Between November 14 and 19, 1963, the price of cottonseed oil futures contracts went down; the object of this litigation is to recover the amounts

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* The Clearing Association, its President, Solomon J. Weinstein, and its Managing Director, David Boyer, were originally named as defendants. Summary judgment was granted in their favor on May 17, 1974, and this decision has not been appealed.

The Exchange did not receive any margin payments; this was the function of the Clearing Association. The Exchange required that its members secure certain minimum margin from their customers for the members' own safety but not for payment over to the Exchange. The minimum requirement (which could be increased in the judgment of the member) was a cash amount per contract or the Clearing Association minimum requirement, whichever was higher (PX 56, Rule 31, JA 303e).

Haupt as broker for Allied paid the Clearing Association in variation margin during that period.

The Role of the Commodity Exchange Authority. Plaintiff deprecates the CEA as "a small agency in the Department of Agriculture." (Br., p. 30.) But it was indisputably larger and more powerful than the Exchange, and it was better equipped to detect and prevent unlawful activity like that of Allied and Haupt. The CEA employed auditors to do surprise audits (the Exchange had no auditing mechanism), and economists to analyze ongoing trading, prices, volume and other market conditions (McMinn, JA 872a-873a). Indeed, the source of the voluminous statistical information on which plaintiff relied at trial was the CEA.

Most important, the CEA knew what the Exchange did not—the exact position of every trader on the Exchange and on all other exchanges subject to its jurisdiction. This information was filed, in code, by traders and carrying members directly with the CEA, and was not reported to the Exchange. Thus, a trader's position was known only to him, his carrying broker, and the CEA (McMinn, JA 872a, 885a-886a).

Moreover, the CEA had a representative on the floor of the Exchange daily, usually at closing, to observe trading (McMinn, JA 853a, 874a). In 1963, he was reporting regularly to the CEA in Washington an analysis of what the Allied-DeAngelis position was in cottonseed oil (JA 880a-881a). From November 12 to November 20, 1963, and probably for several weeks prior thereto, he was teletyping Allied's position daily directly to his superiors in Washington (McMinn, JA 882a-883a, 885a). This representative—T. Reed McMinn—testified at trial that the CEA, with all the confidential information at its command, did not detect the wrongdoing which plaintiff says the defendants, without acess to such information, should have detected in 1963 (McMinn, JA 853a, 876a).

The Events of 1963

The story of the Salad Oil Swindle can be told from many points of view. Plaintiff's brief ignores the viewpoint of Haupt—the alleged victim in this case—and limits itself to a distorted account of the defendants' activities in 1963. We will tell both sides of the story.

A. Haupt's Complicity

At trial, as in his brief, plaintiff understandably chose to avoid mentioning Haupt. Plaintiff called 30 witnesses at trial, not a single one of them from Haupt. The only Haupt employee who testified at trial, Fred Barton, the former manager of Haupt's commodity department, was called as a witness by the defendants. Barton's testimony, plaintiff's admissions made in other litigation (JA 1956a-1969a), and documents from Haupt's own files, told the sordid story of Haupt's relationship with Allied that produced the losses in suit.

1. The Beginning of the Haupt-Allied Relationship (Spring 1963)

In the spring of 1963, Haupt became both broker and banker for Allied, lending Allied money to stimulate brokerage business for itself. Haupt embarked on this relation-

ship because it hoped for large commissions, in the face of clear warnings about Allied.

Haupt had rejected Allied's business in autumn of 1962, and already knew some derogatory information about DeAngelis (Barton, JA 1850a). It acquired more such information in an investigation in spring 1963. A Haupt partner examined a dossier at the Chase Manhattan Bank containing "[illegible]" information on Allied (Barton, JA 1851a). Haupt's inside and outside counsel both advised against taking on Allied as a customer; outside counsel warned bluntly: "[DeAngelis] is a crook" (Barton, JA 1858a). Barton told "Skipper" Haupt, a partner of the Haupt firm, that DeAngelis "wasn't mindful" of restraints or restrictions imposed on him (Barton, JA 1854a-1855a).

Most alarming of all, DeAngelis refused point-blank to let Haupt check the authenticity of export contracts to be used as collateral for Haupt loans to Allied (Barton, JA 1853a-1854a), and Haupt acquiesced (Barton, JA 1857a). If Haupt—the only party who had possession of these contracts—had confirmed them, as good sense dictated, it would have discovered they were phony (DeAngelis, JA 1104a) and exposed the swindle.

But "Skipper wanted business" (Barton, JA 1852a) and so did the other Haupt partners. A Haupt sales representative told Haupt partner David Teiger that gross annual commissions from the account "would probably run close to $700,000," and that Allied "will be of assistance in making this firm a major commodity house." (DX 13, JA 1091e-1093e). The projected minimum commissions on the

Allied account were more than twice the total gross business of the entire Haupt Commodity Department (Barton, JA 1841a-1842a). Haupt accepted the account.

2. May 23 to November 14, 1963

A Letter of Intent between Haupt and Allied, providing for various categories of financing by Haupt, was signed on May 23, 1963 (DX 15, JA 1095e-1103e). Thereafter, Haupt's dream of expanded income was realized. In only a few months as Allied's broker, gross commissions earned on this one account were approximately $630,000 (JA 1967a). For the period October 1 to 31, 1963, commissions on the Allied account equaled 13.4 percent of Haupt's total gross income (JA 1967a). For the period November 1 to 15, 1963, Allied's commissions were approximately one-third of the total for the entire Haupt firm (JA 1967a-1968a). Also, by November 15, 1963, Haupt had earned interest on Allied export loans of $98,000 (JA 1967a).

In the course of making this money, Haupt ignored additional warnings of the danger it faced. It financed DeAngelis and bought cottonseed oil futures for him, far beyond the limits of the Letter of Intent and of sound business practice; and it became Allied's chief accomplice in creating the situation which destroyed Allied, Haupt, and the cottonseed oil futures market.

Beginning in July 1963, Haupt's commodities department, in which Allied was the principal account, was under the direction of Jack Stevens, Haupt's controller. Barton was Stevens' subordinate; Stevens assumed the functions of the Haupt partners to whom Barton had previously

reported (Barton, JA 1836a-1845a), and overruled or ignored Barton's counsels of caution. Plaintiff lamely tries to distinguish between Haupt and Stevens on the ground that Stevens was not a Haupt partner himself. But he was, as plaintiff himself said in a suit against Haupt's fidelity insurer based on Stevens' "dishonest, fraudulent and criminal" acts, "a trusted key employee of Haupt . . . the senior employee below the partnership level for the entire 'back office' of Haupt, responsible for the activities of several hundred employees" (DX 5, JA 1011e, 1015e-1017e). Plaintiff also admitted that "the Haupt partnership acquiesced in [Stevens'] responsibility with respect to the handling, operation and supervision of the Allied accounts" (JA 1956a-1957a).

In short, the acts of Stevens were the acts of Haupt, and while the distinction between a partner and an employee may have been significant in plaintiff's fidelity bond litigation, it is insignificant here. It is just one more bizarre aspect of plaintiff's theory that he asks defendants to compensate Haupt for injuries caused by Stevens' dishonesty.

From July 1963 until the November debacle, Stevens received daily reports telling him, among other things, the exact size of Haupt's position (Barton, JA 1846a-1849a; JA 1957a-1958a). Haupt also knew the amount of credit being extended by it to Allied and the security held against those loans. Haupt kept this information to itself and never disclosed it to the Exchange.

Stevens received early warnings of trouble with the Allied account:

—In July 1963, Haupt began accepting soybean oil bills of lading for Allied, and Allied avoided payment for months thereafter; Barton warned Stevens that Allied was "stalling" (Barton, JA 1866a-1867a).

—In August 1963, Stevens asked Barton how far vegetable oil markets were likely to decline, and what was considered the maximum position that a brokerage firm should carry for one customer—questions that reflected Stevens' awareness that Haupt's trading on behalf of Allied could be dangerous (Barton, JA 1868a). But he ignored Barton's response—that the market could go down 2½ cents,* and a position should not exceed about five percent of the open interest (Barton, JA 1868a).

—In early September 1963, DeAngelis approached Barton with a soybean deal which would have enriched DeAngelis personally at the expense of Allied. Barton rejected the proposal as a "fraud," and reported the conversation to Stevens with the comment: "This is the measure of the man you are dealing with." (Barton, JA 1871a-1873a).

Despite the warning signs, Haupt continued buying for, and lending to, Allied on an ever-increasing scale. In early September 1973, 2500 cottonseed oil futures contracts belonging to Allied were transferred from another broker to Haupt. Barton expected that Haupt would hold this position only briefly (Barton, JA 1873a-1874a), and the position was indeed liquidated on September 25 (DX 35, JA 1107e-1110e); but on September 27, 1963, Barton entered

* Cottonseed oil furtures prices are sometimes quoted in "cents" per pound and sometimes in "points", 100 points equalling one cent. The limitation on fluctuations in price on the Exchange was 200 points, or two cents, daily.

the hospital, not to return to his office for six weeks—and on September 30, Haupt reacquired the large Allied position it had liquidated (Barton, JA 1880a-1881a). The momentary elimination of that position from Haupt's books permitted Haupt to respond deceptively to a New York Stock Exchange questionnaire, which related to Haupt's financial condition and compliance with the net capital rule as of September 26, 1963 (JA 1965a-1966a).

In mid-September 1963, Haupt began extending loans to Allied in excess of the $2.5 million specified in the Letter of Intent (Barton, JA 1860a). By November 11—the date of Barton's return to the office—loans to Allied had gone up to $13 million (Barton, JA 1860a-1861a). By the time of Allied's bankruptcy on November 19, the total credit extended by Haupt to Allied, including the deficit in Allied's margin account with Haupt, exceeded $34 million (DX 5, JA 1011e, 1020e). When Barton expressed his concern about the growing size of the Allied account, and suggested reducing Haupt's exposure, he was told he had been taken off the account (Barton, JA 1883a-1885a; 1959a).

During Barton's absence from the office, the long position carried by Haupt for Allied went from 2500 futures contracts to 15,000 (Barton, JA 1884a). Haupt facilitated Allied's purchases by accepting collateral from Allied in the form of field warehouse receipts which were later found to be fraudulent or forged.* Instead of cash margin, Haupt even accepted warehouse receipts as security for

* The worthless field warehouse receipts Haupt took from Allied are to be distinguished from the Exchange's registered warehouse receipts. All of the Exchange's receipts were valid and had oil behind them.

margin loans—a device which Haupt called "product margin." In all of Barton's 35 years' experience in the commodity business, he had never accepted "product margin" (Barton, JA 1862a-1863a). Berg had never even heard the words "product margin." As he testified, "Margin to me is cash or securities" (Berg, JA 759a).

"Product margin," as Barton explained, offers only illusory protection. The risk to be guarded against by collateral is a decline in the price of the commodity, but if the collateral is in the same commodity, any price decline also diminishes the value of the collateral (Barton, JA 1863a; Berg, JA 759a-760a; Leuthold, JA 236a-237a).

When Barton returned to the office on November 11, he urged that the Allied account be frozen (JA 1960a). Stevens said he would not do that just yet, because he had given Allied permission to add 800 contracts (Barton, JA 1888a). Eight hundred cottonseed oil futures contracts had a value of more than $6 million.

Haupt disclosed none of these facts to the Exchange. On the contrary, it reassured Berg, the Exchange Managing Director, when he inquired in September 1963, that it knew exactly what it was doing, that it was getting margins in excess of the Exchange's cash minimum, and that it was adequately protected (Berg, JA 744a-747a). In October 1963, when the Clearing Association imposed a more stringent margin requirement, Stevens protested both to Berg and to Solomon Weinstein of the Clearing Association. In response to these protests, Berg and Weinstein warned of the risks inherent in large-scale trading in cottonseed oil

(Berg, JA 794a-797a; Weinstein, JA 476a-477a). Stevens imperiously rejected the warnings.

The new Clearing Association margin requirements were scaled up according to size of position (PX 30, JA 157e). Margin per contract increased with the number of contracts, in the fashion of a progressive income tax. On October 10, 1963, when the new rates were announced (to be effective weeks later), the escalated rates would have required Haupt to put up $2,800,000 in additional margin if the position it carried was not reduced (JA 1958a-1959a). Instead of reducing or distributing Allied's position (which would have reduced Haupt's commissions), Haupt significantly *increased* the position, thus increasing even further amounts of escalated margins it had to pay. As Haupt was receiving payments of variation margin from the Clearing Association, it chose to release all of these funds to Allied, instead of holding back some money for its own safety and protection. These funds were released at a time when the limits of the Letter of Intent were exceeded; when Allied had not even paid Haupt the original margin which Haupt had remitted to the Clearing Association and to its Chicago brokers; and when no provision whatever was made for the escalated margin which Haupt would have to pay (JA 1963a-1964a).

Plaintiff's statements in the fidelity bond litigation described even more reports, warnings and pleas to Haupt for some element of caution (JA 1957a-1962a). These were uniformly ignored. Haupt proceeded in utter defiance into the fateful week of November 14, when its recklessness and avarice culminated in its undoing.

3. *Thursday, November 14 to Tuesday, November 19, 1963*

These days were critical in the history of the Salad Oil Swindle.

On Thursday, November 14, 1963, Haupt learned that the disaster which it had been inviting was at hand. Its daily margin calls upon Allied had previously been met with wired federal funds; on November 14, Haupt instead received three uncertified checks totalling $1,151,000 (JA 1960a; DX 19, JA 1105e-1106e). Haupt did not notify the Exchange or anyone else; Stevens did not even try to deposit the checks, but hid them under his desk blotter where they were found months later (DX 5, JA 1011e, 1023e; JA 1968a-1969a).

On Friday, November 15, Haupt was told by an Allied representative that Allied was having "financial difficulties" (JA 1961a). On the same day, Barton circulated a market letter predicting price declines; he recommended that cottonseed oil and other commodities futures be sold. Stevens asked him how far down the market would go. Barton responded, "two to two and a half cents, provided Tino can meet his margin calls." (Barton, JA 1896a-1897a; JA 1960a.) A decline of this magnitude would have meant a loss of $18 to $22.5 million in the value of the position Haupt carried for Allied (see JA 1898a). Yet Haupt took no action to reduce its position, and did not report its knowledge or situation to the Exchange.

On Saturday, November 16, Haupt was told by Allied that Allied had no solution to its financial difficulties (JA

1961a). Instead of reporting Allied's impending bankruptcy to the Exchange, Haupt obtained one last field warehouse receipt from Allied as additional collateral (Barton, JA 1900a).

On Monday, November 18, Haupt was receiving numerous reports about Allied's failure to meet margin calls and its financial predicament (JA 1961a). In response to Barton's request for instructions before market opening that morning, Stevens said, "*Do nothing.*" Under its agreement with Allied, Haupt had the right to "liquidate [Allied's] account or accounts or any part thereof at public or private sale without notice, call, or advertising of any kind when . . . margins in [Haupt's] judgment are insufficient for [Haupt's] protection, or upon [Allied's] failure fully to respond to any margin call made by Haupt." (Barton, JA 1898a; DX 4A, JA 1009e.) On this day, Haupt increased its net position by 2510 contracts resulting in additional margin of nearly $5 million which Haupt paid to the Clearing Association (Boyer, JA 467a-469a, 471a-472a).

Haupt still preferred to gamble on the market rather than to report its information concerning Allied to the Exchange. In the course of November 18, the market fell an average of approximately 100 points (PX 156, JA 567e).

On Tuesday, November 19, Allied filed a petition in bankruptcy. Only then did Haupt in desperation finally turn to the Exchange and make any disclosure of its situation. Two Haupt partners attended a joint meeting of the Exchange and Clearing Association Boards, and said that Haupt could survive if, but only if, trading were closed immediately (MacDonald, JA 659a; Anderson, JA 1236a-

1237a). Trading was closed and Haupt thanked the Exchange for rescuing it from insolvency. Weeks later, when it was discovered that the warehouse receipts which Haupt had accepted as collateral were worthless, Haupt was driven into bankruptcy.

On November 18, Barton had prepared a complete summary of the Allied account. This summary included the total debt owing by Allied to Haupt, a component of which was the unpaid margin calls through November 18. The existing margin account of Allied with Haupt, including warehouse receipt "product margin," was in excess of the existing debt (Barton, JA 1901a). Even on November 19, the Haupt representatives reported to the Exchange at the meeting on that day that, with the closing out of contracts, and resultant return to Haupt of more than $3 million, Haupt would be able to remain solvent (MacDonald, JA 657a-658a).

The discovery that the field warehouse receipts which Haupt accepted as collateral were forged changed the picture radically. Haupt could not recover its indebtedness directly from Allied, on account of the bankruptcy, and had not provided itself with sufficient collateral against that indebtedness, since it accepted worthless "product margin" from its customer instead of cash.

Plaintiff has admitted that one of the acts which "materially prejudiced" Haupt in the days before November 20 was "allowing Allied to meet its financial obligations to Haupt by delivering warehouse receipts to Haupt rather than making payment in cash" (DX 5, JA 1011e, 1022e).

Haupt had no procedure for verifying the field warehouse receipts it was accepting from Allied (Barton, JA 1859a).

Haupt's refusal to take positive action to be ready for the new margin effective November 15; its refusal to take positive action after the receipt of vital information from Allied that Allied was having insoluble financial difficulties; its refusal to take positive action after Allied's failure to meet a margin call; its refusal to take positive action after Allied failed to meet demands on November 18 (DX 5, JA 1011e, 1022e-1023e)—when coupled with Haupt's incredible recklessness in the period prior to November 14—demonstrate that the cause of Haupt's injury was Haupt itself and not any action or inaction of defendants.

B. Defendants' Conduct

Defendants were doing their best to protect the interests of the cottonseed oil futures market. Despite diligent inquiry, defendants did not discover the situation created by the misconduct of Allied until mid-November 1963. When they did discover the immense size of Allied's position, they took prompt and appropriate action.

1. Prior to November 14, 1963

During the period prior to November 14, 1963, when Allied, assisted by Haupt as banker and broker, was building a huge long position in the cottonseed oil futures market, defendants did not know what that position was. Haupt kept Allied's position a secret, reporting it only to the CEA in code. Plaintiff claims that defendants should have made an investigation which would have revealed the position. Plaintiff, on Haupt's behalf, thus is suing defendants for not finding out about Haupt what Haupt already knew but didn't disclose. Even if plaintiff could recover on such a theory, the facts do not support a claim that defendants should have suspected and investigated Haupt sooner. No event prior to mid-November gave defendants cause for alarm, but they nevertheless made extensive inquiries, receiving assurance from every available source, including Haupt, which deliberately concealed the true facts.

(a) *The Absence of Any Cause for Alarm*

The unanimous testimony of every party and non-party witness who was in contact with the cottonseed oil futures market in 1963—apart from DeAngelis and his associates, who had inside knowledge of the Salad Oil Swindle—was that the market appeared normal, stable and orderly. Trading had increased, but that was not in itself a troubling sign, particularly since the United States was producing and shipping a tremendous quantity of edible oils (Berg, JA 740a). There were no drastic price changes (Berg, JA 793a), and prices seemed to be consistent with market conditions and with substitute oils (Fashena, JA 975a). Most significantly, at no time was the market in an inverted pattern of price; that is, contracts for future delivery months were priced successively above each other, indicating no tightness of supply or price abnormality (Berg, JA 697a; Rehders, JA 1024a; JA 1970a). Throughout the year, prices fluctuated normally (DX 1A, pp. 10-14, JA 921e-925e; Fashena, JA 908a-909a).

The market was always highly sensitive to news and rumor (Preston, JA 411a-412a; MacDonald, JA 503a, 510a).

Particularly in the fall of 1963 there were several bullish factors. There was, generally, an indicated sharp pickup in exports of oil by the United States (Preston, JA 413a, 432a; MacDonald, JA 506a; Gray, JA 1756a-1757a). The United States government was shipping great quantities of oil under the Food for Peace Program, and also was buying substantial quantities of oil for school lunch programs (Berg, JA 720a). Until mid-November, there was the persistent and widely accepted prospect that for the first time the Russians would buy fats and oils from the United States. This prospect heightened in the fall upon announcement of large Soviet purchases of Canadian wheat and negotiations for United States wheat. The negotiations were a shot in the arm to the entire commodity price structure (DX 1A, JA 909e, 917e; Preston, JA 413a-415a; Berg, JA 741a; Fontana, JA 450a). Finally, volume was up on all food exchanges in 1973. There was a growing increase in public interest in all commodities (MacDonald, JA 511a, 651a-652a; Fashena, JA 972a-973a; Anderson, JA 1260a).

T. Reed McMinn, an employee of the CEA since 1941 (JA 870a), visited the Exchange and observed trading there on an almost daily basis during 1963 (JA 853a). He was there precisely for the purpose of seeing if the market was orderly, and if there was any sign of manipulation, corner or squeeze (JA 875a). He testified that during 1963 he did not observe any such unlawful activity. Other non-party witnesses with long experience in the business concurred (*e.g.*, Rehders, JA 1004a, 1007a-1008a; Preston, JA 423a). Defendants themselves, some of whom spent several decades in the commodities field, testified that during 1963 they observed no

threat to an orderly market (Berg, JA 713a; MacDonald, JA 638a-639a, 641a-642a; Fashena, JA 965a).*

Apart from the testimony of these eyewitnesses that in 1963 they observed no manipulation, corner or squeeze, not a single complaint of disorderly trading, manipulation, corner or squeeze was received by the Exchange or its committees from any of the Exchange employees, its 400 members, from their firms, customers, or from any other source (Berg, JA 707a-708a, 711a). In the period prior to November 14, 1963, when prices were rising, shorts were compelled to pay variation margin to the Clearing Association. Yet there was no complaint that prices were too high or artificial (Berg, JA 822a), or that oil was hard to get (Preston, JA 431a), or that any position was excessive or threatened the market (JA 714a-716a).

It was assumed, of course, that Allied was active in the cottonseed oil futures market. In 1963, and for several years prior thereto, it was public knowledge that Allied was one of the world's largest exporters and suppliers of vegetable oil (Preston, JA 402a; MacDonald, JA 631a; Berg, JA 717a, 770a-771a; Fashena, JA 978a-979a; Rehders, JA 1005a), and that Allied was doing a booming business as a supplier to the U.S. Government (MacDonald, JA 631a; Fashena, JA 978a). Allied had sold about one billion pounds of oil each year since 1959 (DeAngelis, JA 1051a). As a large exporter of fats and oils, Allied would necessarily do a large futures business to "hedge" its position in

* Anderson testified that in retrospect and in a broad sense there may have been manipulation in 1963 (JA 1255a-1256a). However, *during 1963,* despite his diligence and close attention to the market, he observed no actual or attempted manipulation or squeeze, and no threat to an orderly market (JA 1264a-1266a).

the cash market (Preston, JA 409a-410a; MacDonald, JA 506a). In fact, while Allied's position was unknown to the Exchange and the other defendants, it was reported to the CEA which after investigation accepted DeAngelis' assurances that he was buying futures to hedge against sales transactions in the cash market. In its publicly released statistics, the CEA classified Allied as a hedger (Dahl, JA 313a-314a).

In the face of testimony from the eyewitnesses, including the government observer, that there was no reason for concern until mid-November 1963, plaintiff relied chiefly on the hindsight testimony of "experts." Plaintiff's experts, raking the ashes of a dozen long years, emphasized alleged statistical "warning signs": increasing volume of trading, a growing open position, an increase in positions reported as hedges by large traders, an increase in ex-pit transactions and an increase in deliveries. These, they said, defendants should have recognized as signs of manipulation (Dahl, JA 263a).*

Defendants' expert witness, Professor Henry B. Arthur of Harvard, testified to the contrary (JA 1826a-1829a), and even plaintiff's witnesses conceded that the alleged "warning signs" were ambiguous at best, could be readily explainable on the basis of ordinary commercial transactions, and were even signs of a healthy market (Leuthold, JA 233a, 234a-235a; Dahl, JA 377a-378a; Gray, JA 1751a).

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* Plaintiff never proved that there was actually a manipulation back in 1963, despite the "facts" set out in his Brief (pp. 12-15). There was no evidence of the artificiality of any price during 1963, proof which would be essential to a price manipulation (Gray, JA 1752a-1754a, 1769a; Dahl, JA 262a). Plaintiff's experts were not even asked to do any price analysis (*e.g.,* Dahl, JA 316a-317a).

Professor Reynold P. Dahl, one of plaintiff's experts, admitted that the first three "warning signs," the only three which were readily available in government publications, would be insufficient even to call for an inquiry (Dahl, JA 337a, 345a). The other alleged "warning signs" were statistics that no one thought important enough to compile or publish during 1963. In short, the "warning signs" doctrine was exposed at trial as an obvious invention for litigation purposes. (See Fashena, JA 976a-978a, 993a-994a). Indeed, plaintiff's chief witness, Professor Gray, wrote in 1964 that a manipulation can be detected only by hindsight (DX 215, JA 1279e-1289e).

No commentator or expert in 1963, including the CEA, felt that the market was manipulated or in danger of becoming disorderly. On the contrary, plaintiff's "warning signs" were perceived at that time as evidence of a healthy market. The increases in volume, open interest and concentration seemed readily attributable to the bullish news, the heavy flow of the crop (Fashena, JA 972a), and the large expansion in activity on commodities futures market generally (*e.g.*, Fashena, JA 972a-973a; Anderson, JA 1259a-1261a). Since both the short and long interests were concentrated in large traders, there was a belief that the shorts were trade shorts with oil to deliver and the longs were trade buyers with contracts to fill in the export market (MacDonald, JA 529a; Fashena, JA 977a).

The number of deliveries increased with the rise in volume and open interest, although the percentage of deliveries as against volume on the Exchange in 1963 remained about the same, and within the range plaintiff's expert defined as "average" (Dahl, JA 347a-350a, 375a-

376a). Plaintiff's witness, Professor Dahl, ackowledged that on exchanges with which he is familiar, there have been sharp increases in volume, open interest, shifts in distribution of commitments of traders, and deliveries, and in the context of the market, these are not unhealthy signs (JA 379a-382a). There was no historical percentage of contracts settled by delivery on the Exchange (Preston, JA 422a). The increase in deliveries in 1963 was not a disturbing fact but was seen as a confirmation that the market was serving a real economic function (Fashena, JA 973a).

The fact that new warehouses were being built and licensed (which indicated that trade interests sensed a lasting expansion in volume of trading, use of the futures markets and exports) (Fashena, JA 974a) made it logical that deliveries and ex-pits would increase, since these were the only ways to tender oil on the Exchange (Anderson, JA 1182a-1183a, 1261a-1262a).

Since Haupt itself was involved in more ex-pit transactions in the fall of 1963 than anyone else—more indeed than all of the defendants *combined* (Gray, JA 1748a-1749a, 1758a)—plaintiff's argument that the ex-pits were evidence of some evil afoot which the Exchange (but not Haupt) should have known or detected is topsy-turvy. In letters pertaining to every one of its ex-pits, as they were made, Haupt represented to the Exchange that these were all legitimate transactions (DX 35, JA 1107e-1110e).

Ex-pit transactions were entirely proper, specifically sanctioned by Section 4 of the Commodity Exchange Act and Rule 6 of the Cottonseed Oil Futures Contracts Rules of the Exchange (PX [illegible]6, JA 303e). Both the statute and the rule permitted ex-pits in unlimited quantities and unlimited

frequency. Ex-pit transactions served a recognized need in the market, in that they could be used for either movements of position without change of ownership or exchanges of futures in connection with cash, which as a practical matter could not be accomplished as effectively in the ring (Fashena, JA 905a-906a, 989a-991a, 995a-996a; Dahl, JA 352a-360a). The volume of ex-pits seemed commercially logical in 1963 and no unlawful activity was discerned (Fashena, JA 975a; MacDonald, JA 648a). Where the Exchange had any question as to particular ex-pits, it investigated until it received satisfactory assurances as to their legitimacy (Anderson, JA 1244a-1245a, 1246a-1247a; JA 803a-804a).

Nevertheless, plaintiff expended much time and effort on the complexities of the ex-pit transactions which Allied engaged in with other firms in the vegetable oil industry, including Bunge and Continental. Plaintiff succeeded in demonstrating what no one denied—that the ex-pit transactions had served a financing function. Plaintiff also succeeded in getting Professor Gray to testify, from hindsight and without any price analysis, that the transactions served Allied's undisclosed purpose of preventing a drop in the price of cottonseed oil (Gray, JA 1665a). Professor Gray labeled the transactions manipulative (Gray, JA 1652a-1653a), but Professor Arthur disagreed (Arthur, JA 1825a-1826a, 1832a). Moreover, there was no evidence presented to show that the Exchange or any of the defendants—most of whom were wholly uninvolved with the ex-pit transactions—should have detected such an alleged manipulation. Indeed, plaintiff's witness DeAngelis testified that he deliberately concealed his manipulative intent from defendants (DeAngelis, JA 1111a).

The most devastating testimony on the ex-pits was given by McMinn, the CEA representative. He testified—with the support of documentary evidence (PX 41, JA 159e-169e)—that he was aware of the transactions when they took place; discussed them with Berg; was aware that they were used for financing; was aware of specific aspects of the transactions questioned by plaintiff—and saw no reason to question them in 1963, or indeed thereafter (McMinn, JA 866a-867a, 855a-865a, 878a, 887a-890a).

The jury was entitled, we submit, to weigh McMinn's impartial testimony more heavily than the after-the-fact theorizing of plaintiff's witness Professor Gray.

The other evidence on which plaintiff relied in contending that defendants should have been gravely concerned before November 14 was even more tenuous. Plaintiff contends that defendants should have been alerted to a manipulation by Allied's buying at the close (Br., p. 14). But there was always a flurry of activity in the last minutes of trading on the Exchange (Fontana, JA 452a). Buying at the close, in full view of the CEA representative on the floor at that time of day, had a legitimate purpose (Berg, JA 790a-792a; Fashena, JA 991a-992a; Rehders, JA 1022a-1023a). Also, there was heavy activity all day long (Preston, JA 416a-417a; Fashena, JA 1003a), so that any such buying was not unusual and did not stand out.

Plaintiff finally stressed two letters in August 1963 from the Clearing Association (PX 27, 28, JA 153e, 155e), which brought to the attention of the Exchange growing concentrations of contracts in the hands of relatively few members of the Clearing Association, without disclosing the identity

of the members or size of the positions. This problem, however, was dealt with by the Clearing Association through an increase in margin requirements (so-called "scale up" margin), imposed with the approval of the Exchange after a meeting to discuss the subject between Association and Exchange representatives (PX 30, JA 157e). The Clearing Association margin automatically became the Exchange's minimum (PX 56, Rule 31, JA 303e).

Plaintiff made no showing that the "scale up" margin was not a reasonable and adequate way of dealing with the concentration problem in the autumn of 1963; and plaintiff's present attack on the margin increase as insufficient contrasts strangely with the protests of Haupt at the time, when it complained to both the Exchange and the Clearing Association in October 1963 that the measure was too stringent. In response to Stevens' complaints on behalf of Haupt, both Berg of the Exchange and Weinstein of the Clearing Association warned Stevens of the risks inherent in large scale trading in cottonseed oil futures—risks which Haupt continued to ignore (Berg, JA 794a-797a; Weinstein, JA 476a-477a).

(b) *Defendants' Investigations*

Although there was no apparent reason for alarm before mid-November 1963, the Exchange and its officials were wary of Allied and made repeated inquiries to confirm that there was no threat to orderly marketing. Until November 14, the responses were uniformly reassuring. The inquiries included the following:

(1) In July 1963, at MacDonald's suggestion, Berg asked the CEA for Allied's position. Alex Caldwell,

head of the CEA, refused to supply the information, saying that in the absence of a compelling reason, the CEA was legally bound not to give out such figures (MacDonald, JA 520a-523a; Berg, JA 780a). The obvious implication was that no "compelling reason" for disclosure to the Exchange existed—a reassuring fact (MacDonald, JA 635a).

(2) Between July and November 13, 1963, Berg talked to the CEA several times about the open interest, about trading, and about Allied specifically. Berg learned that the CEA had investigated Allied—including Allied's representation that its purchases of futures contracts were for hedging purposes, and that the CEA could not find anything that required bringing charges (Berg, JA 723a-728a; McMinn, JA 893a-894a). At least one of these conversations took place in September or October 1963 (Berg, JA 779a). Again, the CEA reassured the Exchange.

(3) When a large ex-pit transaction transferring contracts from a broker named Ralph N. Peters to Haupt was reported, Berg asked Peters about it. He was told that Allied had moved its account not because of any problem but presumably, Peters said, because Allied had found that Haupt would do the businesss cheaper (Berg, JA 742a; see Dahl, JA 325a).

(4) Following the Peters-Haupt ex-pit, Berg talked to Milton Goldfogle, a member of the Board of Managers, and also a floor broker who had a close association with Haupt (MacDonald, JA 634a). Goldfogle visited Haupt to confirm that it was handling the account properly and knew what it was doing, and reported this

additional assurance to the Exchange (MacDonald, JA 535a).

(5) Also as a result of the large ex-pit from Peters to Haupt, Berg, at MacDonald's instruction (MacDonald, JA 525a), made arrangements to see Haupt, which was a new face in the cottonseed oil market, though a well-known and respected brokerage house (Berg, JA 709a-710a, 733a).* At a meeting between Berg and Stevens, which took place in September 1963, Berg learned that Stevens was Haupt's Controller, was a certified public accountant with experience in other commodity firms, was in full charge of Haupt's Commodity Department, and seemed to be "fully capable and knowledgeable in commodities." Berg pointed out that vegetable oils could be very volatile, and that a change in price of only one cent meant $600 per contract. Stevens assured Berg he was totally familiar with this market, and that Haupt's capital—already $5.6 million according to its financial statement—would be up a couple of million dollars in December (Berg, JA 745a-747a, 762a).

As to Haupt's handling of the Allied account, Stevens gave Berg similar assurances. Stevens said that he had met personally with Allied and reviewed

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* Plaintiff coyly asserts that Haupt was innocent and inexperienced, that it sought the advice of the Exchange before engaging in ex-pit trading for Allied, and that it got the "green light" to proceed from the Exchange (Br., p. 33). This is an appallingly misleading statement. Haupt's request of the Exchange, by Barton, concerned formal procedures and documentation to be submitted on two ex-pits done by Haupt. It was not an inquiry by Haupt as to whether Haupt should engage in ex-pit trading, how much, or with whom. Haupt never sought or received—and obviously did not await—any "green light" from the Exchange on its ex-pit trading or any other trading for Allied.

all aspects of the account with them; that Haupt was requiring and obtaining full original margins, and keeping the account "marked to market," *i.e.*, that additional margin was posted daily to cover price fluctuations; that original margins had been increased from $400 per contract to $500. Stevens also said he had assured himself that Allied's position was a hedge position (Berg, JA 746a, 754a-755a, 773a; MacDonald, JA 531a). The Exchange thus had the assurance of the CEA and of Haupt that they both had confirmed Allied's position as a hedge, and Allied therefore had a legitimate need for the futures contracts.

(6) After this meeting, again at the suggestion of MacDonald, Berg met with DeAngelis, to learn more about his operation and to confirm Haupt's representations (Berg, JA 775a-776a; MacDonald, JA 534a, 542a). DeAngelis told Berg he was doing a tremendous volume of business and that his position in the futures market served as price protection against his sales commitments and manufacturing needs (Berg, JA 764a-773a).

(7) At their meeting, DeAngelis had informed Berg that he was receiving financing from Bunge and Continental, and complained that they were not giving him as much financing as he would have liked. After talking with DeAngelis, Berg checked with both Bunge and Continental to corroborate that they were extending some financing to Allied (Berg, JA 751a, 753a-754a).

(8) At their meeting, DeAngelis had suggested that Berg talk to Gittleman (Allied's oil trader) about

anything he wished to discuss, including the ex-pits (Berg, JA 778a). Acting on this suggestion, Berg initiated several discussions with Gittleman about the Allied ex-pits (Berg, JA 800a-802a, 805a-807a, 808a). In order that Haupt might satisfy the request of the Exchange, Gittleman furnished the written contracts Allied had entered into as the basis for the ex-pits (*e.g.*, DX 204, JA 1139e-1188e). In each instance, the Exchange was getting letter confirmations from both sides in the ex-pit transactions, and Berg satisfied himself that all the pieces fit together (Berg, JA 802a).

(9) In October, as noted above, Stevens came to Berg to protest the imposition of "scale-up" margin. Berg took the occasion to inquire again into Haupt's handling of the Allied account. Again, Stevens was confident and reassuring; he told Berg that original margins had been increased to $600 per contract, and that Allied was meeting all margin calls (Berg, JA 794a-796a).

(10) At about this time, the Exchange called in its warehouse receipts for revalidation. The Exchange determined that every one of its receipts was genuine, and had oil behind it (MacDonald, JA 649a-650a).

In addition to Berg's efforts, Anderson, in the September-November period, took it upon himself to check on stories that he had heard that Allied was a large buyer of oil. His inquiries included the following:

(1) Anderson asked a CEA representative if the CEA was aware of the stories about Allied. The response was: "Don't worry, we are watching it very closely, on a day to day basis, and so far as we can see everything is all right." (Anderson, JA 1195).

(2) Anderson spoke to a representative of Morgan Guaranty Trust. That representative assured Anderson that one of its clients was lending to Allied and had good collateral (Anderson, JA 1195a).

(3) Anderson made an inquiry of another company dealing in edible oils. The inquiry yielded the information that the company's experience with Allied was satisfactory (Anderson, JA 1196a).

(4) Anderson spoke to Richard Forti of Bunge, which dealt with Allied in oil exports. Forti told Anderson that he saw no reason to believe Allied was in any difficulty (Anderson, JA 1196a).

(5) The Credit Department of Merrill Lynch sought for a customer a bank reference on Allied. The report was favorable (Anderson, JA 1196a).

(6) In November, Anderson asked the Merrill Lynch Credit Department to make a credit check on Allied. On November 18, 1963, Merrill Lynch received a reply from the Chase Manhattan Bank—one of Haupt's principal creditors—saying that Allied's credit was "excellent." (Anderson, JA 1269a-1270a).

In short, none of the inquiries suggested any need for intervention in the free market prior to mid-November 1963. It was not until then that Anderson's persistent digging produced information which troubled him. He learned that, based on weather reports from the Soviet Union, it appeared unlikely that the Russians would, as had been rumored, buy substantial amounts of vegetable oil (Anderson, JA 1197a).

If the rumors of a Russian purchase were indeed false, Anderson wondered what could justify Allied's rumored large-scale buying, and he asked Merrill Lynch's research department in Chicago to estimate, based on the best available market information, Allied's position in vegetable oils, both soybean and cottonseed (Anderson, JA 1197a-1198a). When he heard on November 13 that Allied's position might be in the neighborhood of 50% of the open interest, Anderson became concerned, and expressed this concern to Klein, a fellow member of the Exchange Executive Committee; Anderson and Klein then went together to see Berg, who called the CEA to repeat his request for Allied's position (Anderson, JA 1198a, 1203a-1205a; Klein, JA 1389a, 1391a, 1393a-1394a).

When the requested information was supplied on the following day, November 14, the Exchange learned for the first time that Allied held 90% of the open long position in cottonseed oil futures trading. At that moment, Haupt held almost all of Allied's contracts.

2. Thursday, November 14 to Tuesday, November 19, 1963

Plaintiff's claims of bad faith regulation were concentrated in this period when, he alleges, the market was kept open in order for defendants to benefit themselves.

Four business days elapsed between the first disclosure of Allied's position to Exchange officials on Thursday morning, November 14, and the termination of trading on the Exchange after the close on Tuesday, November 19. The closing of the market—done at Haupt's request to save it from bankruptcy—was a drastic step; we know of

no other case where an exchange was closed to bail out a member who had become overextended. Still, plaintiff claims that the brief interval before the decision to close trading was too long—that the Exchange should have closed trading and settled contracts the instant it learned the size of the Allied-Haupt position on November 14, thus protecting Haupt against the consequences of the ensuing price declines. Not even plaintiff's own expert witnesses would endorse this argument (Gray, JA 1768a; Farris, JA 2028a).

Plaintiff claims that cottonseed oil futures were manipulated upwards to artificial levels prior to November 14; if that is true, to close trading and settle contracts on the basis of prices on that day would have given Allied and Haupt the full benefit of their manipulation. Professor Gray, plaintiff's chief expert witness, thought this would have been improper (JA 1768a). No rational justification was advanced for closing the market and settling contracts at prices prevailing on November 14.

Having no basis to support what plaintiff says defendants should have done, plaintiff attacks what defendants in fact did as "ludicrous" and a "virtual farce" (Br., pp. 35, 50). None of plaintiff's experts, who had twelve years to reflect on the matter between the events in suit and the time of trial, was able to suggest an alternative course of action; one of the experts, Professor Paul Farris, testified that he had studied the problem for years, and still did not know what the defendants should have done (Farris, JA 2028a-2029a).

Defendants' actions were entirely reasonable, in light of the facts before them, as a day-by-day review demonstrates.

November 14, 1963

On Thursday, November 14, Berg learned from the CEA, and told MacDonald, that Allied held an enormously large position. However, there was no reason to expect that prices would drop or that, if they did, Allied and Haupt would be unable to meet their obligations (MacDonald, JA 553a-554a, 556a, 610a-612a; Fontana, JA 454a-456a; Berg, JA 758a; Fashena, JA 982a; Rehders, JA 1009a). Indeed, the Exchange had been led to believe—by Haupt among others—that Allied was hedged, so that any loss in its futures position would be offset by gains in the cash market. It did not seem that disaster was at hand; the Exchange did not know, because Haupt did not tell it, that Allied had met its margin call of that day with worthless checks, or that Allied's position was being financed by "product margin" (see pages 18-19 above).

While on November 14 the danger of a corner or squeeze* seemed highly unlikely in view of the enormous supply (MacDonald, JA 587a; Berg, JA 817a, 818a; Ander-

* Plaintiff's concern about a potential squeeze (Brief, p. 36 fn.) is both curious and baseless. In view of the overwhelming supply of oil in 1963 (*e.g.*, Anderson, JA 1266a-1267a; Fashena, JA 968a-970a), which could have quickly and easily been put into deliverable grade (MacDonald, JA 588a, 594a, 595a-597a; Anderson, JA 1266a-1268a; Fashena, JA 966a), there was no threat of a squeeze. The ultimate proof is that no one was scrambling for oil (Anderson, JA 1268a-1269a; MacDonald, JA 641a; Rehders, JA 1007a), and there was no need to pay any premium to get oil. The fact that nearby deliveries were selling at a discount under distant months was a conclusive indication that supply was comfortable and there was no squeeze (Rehders, JA 1024a; Fashena, JA 966a).

The danger of a squeeze, moreover, would have been that Allied, the predominant long, could have taken advantage of the shorts' inability to get deliverable oil and force them to buy from Allied at artificially high prices (Br., p. 36). Any failure to act thus would have hurt the *shorts,* not Allied or its broker, Haupt. This unfounded complaint is therefore a curious one to be raised by Haupt's trustee.

son, JA 1266a), even if Allied's position posed such a threat, there were still approximately five weeks to make delivery on the near-month contracts. Therefore, sufficient time would have remained to deal with such a threat (MacDonald, JA 597a). Indeed, if a squeeze was in progress, prices would have gone up and not down.

The Exchange's goal on November 14 was to try to arrange an orderly liquidation of the Allied position, without creating a panic. To avoid panic, the exact size of Allied's position was not disclosed, even to the Exchange Board of Managers or all of the defendants; the document showing the position (PX 1, JA 1e) was locked in a safe (MacDonald, JA 576a-577a; Berg, JA 819a-821a). To achieve an orderly liquidation, a control committee was appointed, and a request for members of the Exchange to furnish the positions of their customers to the control committee was sent out (MacDonald, JA 563a-569a, 573a).

Plaintiff argues that the "position call" sought only information which Exchange officials already knew; this is false. The document supplied by the CEA listed only the position of traders, and did not show which broker, or how many of them, carried the position.* As explained at trial,

* As McMinn of the CEA testified, any time the CEA "sees a considerable large position, it alerts [them] to the possibility of something occurring and going further into the situation to get all the data [they] feel necessary to arrive at whether or not a manipulation is potential or has occurred." (McMinn, JA 891a). According to Mr. McMinn, the information on PX 1 would not be enough to reach any conclusion about a manipulation, squeeze or corner; you would need a lot more information (McMinn, JA 892a). Thus, PX 1 was not the culmination but the beginning, of an inquiry.

The Clearing Association knew only the net position of its members, and would have had to do its own position call to get the required data (Boyer, JA 464a, 465a-466a).

an orderly liquidation, without panic, could only be accomplished through discreet inquiries to brokers who were members of the Exchange. Direct communication from the Exchange to the traders would have been counterproductive (MacDonald, JA 577a-580a, 653a). As plaintiff's expert witness Professor Dahl testified, since positions are such a highly guarded secret, a position call is extremely sensitive (Dahl, JA 399a-400a). Discretion also led the Exchange to make its position call by mail rather than by telephone; a series of telephone demands by the Exchange that members furnish their positions immediately might well have produced the panic which the Exchange sought to avoid. The appointment of a control committee and consequent position call were entirely reasonable and appropriate means for the Exchange to pursue its inquiry. Appointment of a control committee was a step which the Exchange used effectively on at least two prior occasions (Berg, JA 728a-729a), and a step which had been used many times on many other exchanges (McDonald, JA 654a).

On November 14, Anderson spoke by telephone with Caldwell, head of the CEA. He asked Caldwell, "What in the devil do you do with a market where one interest controls 90 percent of the long side?" Caldwell said that while liquidation at a fixed price might ultimately prove necessary, "that is a very dangerous thing to do and could have bad implications not only for the Produce Exchange but for all commodity markets in general." Caldwell said it was certainly worth exploring the possibility of arranging a takeover of the position (Anderson, JA 1209a-1210a, 1271a).

November 15, 1963

The position call went out on Friday, November 15, 1963, calling for a response by the following Wednesday, November 20. The market declined only modestly on November 14 and 15 (PX 156, JA 567e), and there was every reason to expect that a response to the position call by November 20 would permit the control committee to work out an orderly voluntary liquidation. Plaintiff argues that three days' notice was too much time, yet Haupt itself did not complete its response until November 22, 1963 (PX 18e, JA 85e-87e).

On November 15, as on November 14, there was no reason to believe that catastrophe faced the Exchange or any of the other parties, and no reason to abandon the reasonable course which had been adopted by the Board of Managers just the day before.

The reasonableness of the Exchange action was further confirmed by telephone conversations that day with Caldwell. In the first conversation, Caldwell told MacDonald that he was fearful of a corner, which both MacDonald and Berg thought impossible in view of what they knew about the size of the new crop, the competitive oils and the vast surplus (MacDonald, JA 585a-586a, 587a; Berg, JA 817a-818a). MacDonald told Caldwell that the Exchange had appointed a control committee. Caldwell said he thought this was a good idea, and very much worth a try (MacDonald, JA 586a). In a second call that day, Caldwell reported that the Undersecretary of Agriculture had asked him to remind MacDonald that if the Exchange didn't carry out its obligations to preserve an orderly market,

they had power to bring charges against the Exchange (MacDonald, JA 600a-601a). But in neither conversation did Caldwell or the CEA criticize the action it knew was being taken by the Exchange or recommend an alternative program. Caldwell did not mention closing the market (MacDonald, JA 655a).

Monday, November 18, 1963

On Monday, November 18, there was the first sizeable price movement in months (MacDonald, JA 614a)—a drop of about 100 points, which was still well within the long-established 200-point daily fluctuation limit on the Exchange, and less than Barton had predicted. Plaintiff urges that the price drop occurred because Allied stopped buying. It is at least as significant that the widely touted expectation of Russian oil buying, which had been a principal bullish factor, was discounted at this time (MacDonald, JA 608a-609a; Berg, JA 829a-830a). Haupt itself in its market letter predicted the downtrend and advised selling. On this day also, Haupt apparently was endeavoring to sell off the position privately, which would have depressed the price (DeAngelis, JA 1114a-1120a). Finally, there was a rumor that Haupt had rejected trades made for Allied, another price depressant (MacDonald, JA 656a).

Still, there was no reason to believe that imminent disaster awaited the Exchange or any other party. However, the Exchange acted immediately in an effort to maintain the *status quo* until answers to the position call were received (MacDonald, JA 581a-582a). The Executive Committee voted to impose a 25-point limitation on price fluctuation, effective the next morning (PX 13b, JA 65e). There

can be no doubt that the imposition of a 25-point limit favored the holders of the long position (Haupt-Allied) and hurt the shorts, who would have benefited from an unfettered price decline.

Late in the afternoon on November 18, Berg advised Caldwell of the 25-point limit. Berg asked Caldwell if, assuming it became necessary and the Exchange could arrange it, the CEA would have any problem with an office trade. Caldwell said he thought that could be arranged (Berg, JA 818A, Tr. 2231).

November 19, 1963

On November 19, the picture changed radically with Allied's filing of a petition in bankruptcy.

On November 19, Anderson, at the request of two Haupt partners, made extensive efforts to have one or more cash commodity firms assume the position carried by Haupt for Allied (Anderson, JA 1226a, 1230a).* When this proved unsuccessful, Anderson suggested that Haupt sell Allied's soybean oil futures on the Chicago Board of Trade in the hope this would facilitate liquidation of cottonseed oil futures and, since Merrill Lynch had already accepted a prior order, Anderson put Haupt in touch with Bache & Co., through whom such sales were effected (Anderson, JA 1234a-1235a).

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* Even on November 19, the CEA (through Robinson) indicated that if a takeover of the position could be arranged they would be all for it (Anderson, JA 1240a). Even on November 19, the CEA was not instructing the Exchange to close out trading or liquidate the contracts.

A joint meeting of the Executive Committee of the Exchange and the Clearing Association was convened on November 19, attended by two representatives of Haupt. The Exchange for the first time learned that Allied's position was not spread among several clearing members, but was concentrated in Haupt, and that Haupt's solvency was threatened (Anderson, JA 1237a). The Haupt representatives told the Exchange that Haupt was adequately protected by collateral and could survive if the market was closed at once (MacDonald, JA 659a; Anderson, JA 1236a-1237a). Defendants thus faced a choice: they could close the market and bail out Haupt, or they could let events take their course. Despite the protests of shorts—who, after paying out margin for months while prices went up, thought they were entitled to benefit from a price decline (Fashena, JA 986a; MacDonald, JA 668a)—defendants, with the concurrence of most of their fellow Board members, decided to close the market.

Strangely, plaintiff now argues (Br., p. 43) that defendants were wrong to consider the prospect of Haupt's insolvency in arriving at their decision. But it was clearly proper and reasonable for defendants to consider the prospect that, if Haupt defaulted, the losses which Haupt brought upon itself would be shifted to innocent traders, many of whom faced ruin (PX 16f, JA 69e-72e). The decision to close the market was formally ratified by the Exchange Board of Managers the following morning, November 20.

Trading was suspended and contracts settled at prices determined in precise relation to soybean oil prices on the Chicago Board of Trade, which, as plaintiff acknowledges,

moved in parallel fashion at all times (Br., Appendix I, I-a). The historical price difference between the two oils was determined (cottonseed oil generally traded at a higher price than soybean oil), and this difference was applied to the closing price of soybean oil on November 19 (MacDonald, JA 670a-671a). Settlement at those prices resulted in the return to Haupt of $3,158,000 of margin on deposit with the Clearing Association (Berg, JA 831a).

At the November 19 meeting, the Haupt representatives expressed their gratitude and appreciation for the action of the Exchange, which—until it was discovered that Haupt had accepted forged warehouse receipts from Allied—appeared to have saved Haupt from bankruptcy. The Exchange's action, while beneficial to Haupt, proved to be suicidal for the Exchange. The shorts, who would have profited on a decline but instead had their hedges wiped out overnight, never came back to the Exchange to any meaningful degree (Fashena, JA 986a). The feeling among traders was that the Produce Exchange contract was not a contract (MacDonald, JA 660a). As plaintiff's experts recognized, the action of the Exchange was unprecedented (Leuthold, JA 232a, 240a; Dahl, JA 383a-384a), and the Exchange trading volume thereafter declined radically, down to zero (Dahl, JA 383a-385a).

The Recovery Sought in This Action

Plaintiff's brief obscures the nature of the injury for which plaintiff seeks recovery in this action. It is understandable why plaintiff, in a 101-page brief with long factual appendices, prefers not to discuss his theory of injury. The recovery which plaintiff seeks represents the market losses

Allied suffered between November 14 and 19 when the market, after rising in the prior months, declined.

But Haupt did not suffer any losses in its own right from this market decline; the losses were those of its customer, Allied. Allied's losses became Haupt's losses because Haupt failed to get cash margin payments from Allied and the security it chose to accept without verification proved worthless.

The Conduct of the Trial

Plaintiff's conduct of the trial, as illustrated by the following examples, reflected his awareness that only confusion and prejudice could save his case.

—Plaintiff's theory of liability changed as his own witnesses exculpated defendants. Throughout the first few weeks of trial, plaintiff seemed determined to demonstrate to the jury that defendants had permitted a corner in the cottonseed oil futures market. In the middle of trial, to the court's surprise (JA 1070a-1071a, 1081a-1082a), plaintiff disavowed any such contention.

—Plaintiff offered clearly inadmissible evidence in an attempt to prejudice the jury. He offered a book entitled *The Great Salad Oil Swindle* (PX 248 id., JA 241-242), an offer which could not possibly have been made in good faith. (The book now appears in plaintiff's brief on appeal among his "Authorities.")

—Plaintiff offered a mass of oversimplified charts and statistics—many of which were admitted as the District

Court gave plaintiff a generous opportunity to prove his case (JA 260a; PX 122-127, 133, 140-42, 156, 158, JA 507e-527e, 535e, 541e-545e, 567e, 569e). Not content with this, plaintiff unsuccessfully sought to show his charts to the jury by means of an overhead projector. The only possible effect of these exhibits was to obscure a key issue in the case—what information was known at what times to which defendants—by creating the illusion of a market in which the statistics selected by plaintiff were instantly available to everyone.

—Plaintiff burdened the record with extensive exhibits and testimony admissible, at best, against only one or two defendants, and which therefore required limiting instructions. Indeed, plaintiff sought to introduce, through the testimony of DeAngelis, a highly inflammatory account of a 1962 incident in which Bunge allegedly discovered that certain of Allied's warehouse receipts were of doubtful value. This incident was irrelevant but highly prejudicial; Bunge and Klein, against whom plaintiff sought to offer the evidence, had already settled another lawsuit by plaintiff based on the same incident (JA 1011a).

Despite plaintiff's efforts, the jury concluded that plaintiff had no case. Plaintiff now asks this Court to let him try again.

ARGUMENT

POINT I

The case should have been dismissed without being submitted to the jury.

Plaintiff, on this appeal, attacks at great length the District Court's conduct of the trial—its granting of partial directed verdicts where there was a complete failure of proof, its rulings on evidence and its charge to the jury. As we shall demonstrate below, these attacks are unfounded. The District Court did not err in directing a verdict against plaintiff on his claims of bad faith, and indeed should have gone further and granted summary judgment or a directed verdict as to *both* counts of plaintiff's complaint, because this lawsuit, brought on behalf of a wrongdoer for an alleged failure to prevent its own wrongdoing, is inherently illogical, unjust and contrary to law.

A. Count I: Commodity Exchange Act Claim

Plaintiff's claim against defendants under the Commodity Exchange Act should have been dismissed before trial, or at least before submission to the jury, for four reasons: (1) Haupt's misconduct bars its recovery; (2) even apart from Haupt's culpability, Haupt has no right of action under the Commodity Exchange Act; (3) defendants did not violate the applicable standards of conduct; and (4) no act by any defendant was the proximate cause of plaintiff's injury.

1. Haupt's Culpability Bars Plaintiff's Claims.

Plaintiff does not and cannot dispute that he stands in the shoes of Haupt and has no greater rights than Haupt would have in this action. Nor does plaintiff dispute the central fact in this case: Haupt's culpability clearly exceeded any culpability that could possibly be imputed to the defendants. Haupt actively participated in, concealed and lied about the alleged "manipulation" which plaintiff says defendants should have discovered earlier. Haupt was largely responsible for creating the large concentration of contracts which plaintiff says defendants should have responded to with stronger and prompter regulatory action. This is, in short, a case of the criminal suing the policeman for the policeman's alleged failure to prevent the crime.

Under the usual principles of tort law, private equities bar a plaintiff from recovery where the plaintiff is equally or more culpable. Plaintiff, relying on cases typified by *Pearlstein* v. *Scudder & German,* 429 F.2d 1136 (2d Cir. 1970), *cert. denied,* 401 U.S. 1013 (1971), contends that this case should be an exception to the general rule because the private equities are outweighed by the public interest in enforcing the Commodity Exchange Act (Br., p. 86).* What plaintiff forgets, however, is that Haupt was not a

* In denying defendants' motions for summary judgment, the District Court accepted plaintiff's contention, citing *Pearlstein* and *Nathanson* v. *Weis, Voisin, Cannon, Inc.,* 325 F. Supp. 50 (S.D.N.Y. 1971); *Seligson* v. *New York Produce Exchange,* 378 F. Supp. 1076 (S.D.N.Y. 1974). At trial, however, the District Court expressed doubt as to its prior holding (JA 2096a-2097a). It submitted the issue of Haupt's misconduct to the jury (JA 2115a-2116a), and reserved decision on whether to grant defendants' motions for a directed verdict on the ground that Haupt's own misconduct was the cause of its loss (JA 2094a-2095a). The jury's verdict mooted this issue.

public investor like the plaintiff in *Pearlstein.* Haupt was a regulated broker registered as a futures commission merchant pursuant to the Commodity Exchange Act, and Haupt's misconduct itself posed a grave threat to the operation of the federal regulatory scheme. Thus, public policy as well as the private equities preclude rewarding Haupt for its misconduct. The Commodity Exchange Act, which has no express private right of action, was never intended to confer standing on a wrongdoer, such as Haupt, to sue an exchange for failing to detect and prevent its own accumulation of contracts. See the discussion at pages 59-60 below.

A commodity futures broker plays an essential role in the proper functioning of the regulatory system of an exchange. Because traders' positions are highly confidential and are not disclosed to the Exchange, the broker is the only member of the Exchange community who at all times knows what his customer's position is. Also, the broker can and is expected to know its customer, its financial stability and trustworthiness. Thus, the broker is uniquely equipped to evaluate the risks—to the customer, to the broker and to the market in general—from a customer's activities. When a broker ignores those risks, as Haupt did in the case of Allied, the regulatory system cannot accomplish its goals.

Pearlstein is in pertinent respects the opposite of this case. In *Pearlstein,* a broker was denied the *in pari delicto* defense when sued by an investor for violation of the margin rules in connection with its extension of credit to the investor. The investor, unlike the broker, did not have responsibility for observing the margin rules, and, indeed,

did not violate the law by accepting excessive credit. The very rationale of the margin rule was that investors could not be permitted to manage their own affairs, and that brokers had the responsibility of limiting credit available for speculation. Therefore, the investor was permitted recovery because of "the salutary policing effect which the threat of private suits for compensatory damages can have upon brokers and dealers. . . ." *Pearlstein* v. *Scudder & German, supra,* 429 F.2d at 1141.*

But the rulemakers felt that the court had gone too far even in the circumstances of *Pearlstein,* and promptly amended the margin rules to prohibit customers from receiving excessive credit. Regulation X of the Federal Reserve System, 12 C.F.R. §224 (1975). A more recent decision of this Court in *Pearlstein* (*Pearlstein* v. *Scudder & German,* 527 F.2d 1141 (2d Cir. 1975)), appears to question whether the original *Pearlstein* decision was correct.

Even assuming that *Pearlstein* is still good law, it cannot be stretched to benefit a broker-plaintiff like Haupt. To permit a guilty broker to shift its losses to an exchange

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* Similarly, in *Nathanson* v. *Weis, Voisin, Cannon, Inc.,* 325 F. Supp. 50 (S.D.N.Y. 1971), the *in pari delicto* defense was denied to a broker when sued by an investor under the securities laws for losses sustained as a result of allegedly misleading inside information given by the broker to the plaintiff. In that case, the broker was said to be the "true insider" with primary responsibility for preventing an abuse of inside information, as opposed to the plaintiff investor, who had violated the law as a tippee, but "whose potential for harm is minimal as compared to that of the original source of the information." *Id.* at 57. Again, the case requires placing upon Haupt the burden of its misconduct here; Haupt was a "true insider" with a demonstrably enormous "potential for harm."

Even in the *Nathanson* situation, the Fifth Circuit has denied the tippee recovery. *Kuehnert* v. *Texs. r Corp.,* 412 F.2d 700, 704-05 (5th Cir. 1969); *see Wohl* v. *Blair & Co.,* 50 F.R.D. 89 (S.D.N.Y. 1970).

would not have a "salutary policing effect"; it would encourage irresponsibility by the very class—brokers—who are the first and indispensable line of defense against improper market activities.

The authorities confirm that brokers who suffer losses by reason of their own dereliction in duty may not present a claim for reimbursement against third parties under a federal regulatory statute. In *Globus* v. *Law Research Service, Inc.*, 418 F.2d 1276 (2d Cir. 1969), *cert. denied*, 397 U.S. 913 (1970), indemnification of an underwriter by the issuer for liability arising under the securities laws was denied; this Court said that the " '*in terrorem* effect' of civil liability . . . might well be thwarted if underwriters were free to pass their liability on to the issuer." *Id.* at 1288. Under *Globus*, if Allied's trustee had made claims against Haupt for failure to curtail and monitor Allied's account—a claim which is no more preposterous than the one asserted here—Haupt could not seek indemnification from the Exchange. It is an *a fortiori* case that Haupt cannot bring an independent suit for the Allied market losses which it absorbed when the collateral it accepted from Allied proved worthless.

In *Herzfeld* v. *Laventhol, Kreksiein, Horwath & Horwath*, 378 F. Supp. 112, 135-38 (S.D.N.Y. 1974), the court refused to permit defendant accountant to shift its liability in connection with issuance of a misleading audited financial report to a jointly culpable underwriter through indemnity. The court also refused to permit the underwriter to recover from the accountant on its fraud claim asserted

as assignee of the claims of innocent purchasers against the accountant. The court said:

> "If the defense of *in pari delicto* is ever appropriate in a securities case, and we think it is, this is such a case. Allen was not a passive investor who merely borrowed money from a bank, or a broker, knowing that the margin regulations were thereby violated. Rather, Allen was an active participant in Laventhol's issuance of a misleading report and sought not only to profit from Laventhol's fraud but to compound it by providing investors with even less information than Laventhol. *It would be absurd and unconscionable to allow Allen to reap a huge profit by asserting the fraud claims of innocent investors when the fraud would never have occurred had Allen acted in accordance with its duty as an underwriter.*" *Id.* at 138. (Emphasis added.)

Similarly, in this case, if Haupt had acted in accordance with its duty as a registered futures commission merchant and a member of the Exchange, and had not made itself the active accomplice of Allied and DeAngelis, the alleged improper actions or failures to act of the Exchange and its directors could never have occurred. To allow Haupt to recover here would be "absurd and unconscionable."

The precise question of the relative responsibility and culpability of a broker and an exchange has recently been discussed in a decision denying the general partners of a brokerage firm standing to sue the New York Stock Exchange for negligent regulation under Section 6 of the Securities Exchange Act, 15 U.S.C. §78f (1964). *New York Stock Excha ge, Inc.* v. *Sloan,* 394 F. Supp. 1303 (S.D.N.Y. 1975). In *Sloan,* the Exchange brought a suit for damages

against the former partners of Orvis Brothers & Co., a defunct member firm, alleging that they had failed to keep accurate records, concealed the precarious financial position of the firm, and conspired to overstate Orvis' net capital position to enable the firm to continue in business despite its failure to meet Stock Exchange net capital requirements. Defendants counterclaimed for loss of their investments, charging that the Stock Exchange failed in its statutory duty under Section 6 of the Securities Exchange Act to enforce Exchange rules, particularly the net capital rule. Defendants asserted that the Stock Exchange had actual knowledge of Orvis' net capital violation and yet affirmatively sanctioned its continued operation, ultimately resulting in the firm's liquidation.

The Stock Exchange moved for summary judgment, dismissing the counterclaims, on the theory that only public customers and not members are within the protection of Section 6. Judge Lasker denied the motion as against the limited partners and subordinated lenders, but struck the counterclaims of the general partners, the persons charged with management of the firm. He held, "The Exchange cannot have failed to enforce the rules unless the general partners failed in the first instance to comply with them, and we believe for the reasons set forth below, that to permit them to assert their counterclaims would do violence to the statutory scheme." *Id.* at 1311.

> "It is of course central to the concept of self-regulation that member firms conduct themselves in accordance with rules promulgated by their governing body. To permit suit by general partners in cases like the present one would do nothing to encourage their careful observance of the rules. To the contrary, it would tend

> to concentrate the responsibility for compliance—and the legal consequences of non-compliance—on a relatively small number of partners, and dilute the protection which the scheme of self-regulation extends to those with a far greater need for it. Even 'passive' general partners are on notice, under hornbook law, that they are bound by the acts of their partners. We see no reason why Congress would have intended to grant them a remedy against the Exchange when the remedy more properly lies against the offending copartner." *Id.* at 1315.

To impose liability on the Exchange, Judge Lasker concluded, would be to "turn the Act on its head."* *See also, Competitive Associates, Inc.* v. *Advest Co.*, CCH Fed. Sec. L. Rep. ¶95,302 (S.D.N.Y. 1975).

Other cases make clear that decisions like *Pearlstein* do not require ignoring a plaintiff's misconduct where that misconduct is itself a significant threat to the stability of a market. Thus, where the plaintiff was not just a sophisticated investor as in *Pearlstein*, but had himself fraudulently induced the defendant bank's violations of the margin rules by means of false representations, conduct "fraught with prejudice to the enforcement of such regulations," plaintiff's action was dismissed on the ground of the *in pari*

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* A footnote in *Sloan*, 394 F. Supp. at 1315 n.16, undertakes to distinguish the District Court's decision on summary judgment in the present case. The distinction, however, is far less persuasive than the remainder of the *Sloan* decision. The court said that regulatory obligations of the New York Produce Exchange under the Commodity Exchange Act were greater than those of the New York Stock Exchange under the Securities Exchange Act. This is a doubtful assertion; but, in any event, the key point is the duty of the broker, whose conduct is critical to the functioning of both regulatory schemes. The *Sloan* court also mentioned the allegations, in the present case, of intentional misconduct—but those allegations, as the District Court found, were wholly unsupported by the evidence.

delicto defense. *Serzysko* v. *Chase Manhattan Bank,* 290 F.Supp. 74, 89-90 (S.D.N.Y. 1968), *aff'd,* 409 F.2d 1360 (2d Cir.), *cert. denied,* 396 U.S. 904 (1969); *see Moscarelli* v. *Stamm,* 288 F. Supp. 453 (E.D.N.Y. 1968). More recently, in *Securities and Exchange Commission* v. *Packer, Wilbur & Co., Inc.,* 498 F.2d 978 (2d Cir. 1974), *aff'g,* 362 F. Supp. 510 (S.D.N.Y. 1973), an investor and broker-dealer which had represented the investor in an unlawful transaction with the defendant brokerage house were both denied recovery on claims against the defendant arising out of the transaction. The court found that an investor who had himself engaged in culpable conduct, and thus the broker claiming on his behalf, were not within the class intended to be protected by the Securities Investor Protection Act. *Id.* at 983-85.

There can be no doubt that Haupt was more guilty of culpable conduct than the defendants, even on plaintiff's theories. Accordingly, any claim on behalf of Haupt under the Commodity Exchange Act is barred by its own misconduct.

2. *Even if Haupt's Culpability Is Ignored, the Commodity Exchange Act Does Not Give Haupt a Right of Action.*

The Commodity Exchange Act provides no private right of action; and although expressly enumerating the duties of a contract market, the Act does not list detection of attempted manipulation as one of them. Section 7(d), on which plaintiff relies, provides only that the Secretary of Agriculture may certify a board of trade as a contract market if its governing board provides for the prevention

of the manipulation of prices or cornering of a commodity (7 U.S.C. §7(d)). The rules of the Exchange, which prohibited manipulation and were binding on all members, including Haupt, met this requirement, and the Secretary certified the Exchange as a contract market.*

Nevertheless, the District Court, by analogy to the more pervasive securities laws held that an implied private right of action did exist. Under the test set forth in *Cort* v. *Ash*, 422 U.S. 66 (1975), the court should have held otherwise and dismissed the complaint.** *Cort* (citing *Texas & Pacific Ry. Co.* v. *Rigsby*, 241 U.S. 33, 39 (1916)) holds that, before a private right of action is read into a federal regulatory statute, it must first be determined that plaintiff is "one of the class for whose *especial* benefit the statute was enacted." 422 U.S. at 78. It cannot be said that the Commodity Exchange Act was enacted to protect futures brokers in the position of Haupt.

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* In contrast, the amendments to the Commodity Exchange Act, 7 U.S.C. §7a, adopted in 1968-1974, provided explicitly that each contract market had a duty to enforce all of its rules and regulations, including those providing for minimum financial standards of members (7 U.S.C. §§7a(8), 7a(9)) and provides penalties for nonenforcement by an exchange of its rules. 7 U.S.C. §13a. The Act also explicitly provides for private rights of action against traders and registered brokers, but not against an exchange. 7 U.S.C. §18.

** *Ricci* v. *Chicago Mercantile Exchange*, 409 U.S. 289 (1973), and *Chicago Mercantile Exchange* v. *Deaktor*, 414 U.S. 113 (1973), are not to the contrary. *Ricci*—like *Silver* v. *New York Stock Exchange*, 373 U.S. 341 (1963)—dealt with classic antitrust claims of boycott, and contained no suggestion that a private right of action by a broker may be implied against a commodities exchange. In *Deaktor*, a claim for failure to regulate was presented under the 1968 amendment which specifically mandated exchanges to enforce their rules. The court stayed the suit pending a hearing by the CEA, and thus did not reach the question whether a private right of action may be implied even under the new law.

3. *Defendants' Conduct Did Not Violate the Applicable Standards.*

Having found an implied private right of action, the District Court held, and instructed the jury, that defendants could be liable for their acts during the period before November 14, 1963 if they acted negligently, and for the period November 14 to 19, 1963 if they were guilty of an abuse of discretion (JA 2110a-2111a, 2113a). In both respects, the District Court was too generous to plaintiff.

Even assuming that a cause of action could exist against an exchange and its directors under the Commodity Exchange Act, defendants could be held liable for the period prior to November 14 only upon a showing that, at the least, they knew and recklessly disregarded facts which should have called for regulatory action, and for the period November 14 to 19 only upon a showing that they acted in bad faith. Since the evidence cannot support a finding of liability for either time period, the court should have held that defendants were not liable as a matter of law.

(a) Before November 14

It is inconsistent both with recent cases interpreting federal regulatory statutes and with practical common sense to permit liability of directors of a commodities exchange or an exchange itself for mere negligence in performing their duties. Particularly where, as here, the Exchange was a nonprofit corporation and its directors served without compensation, it would be unfair to expose them to multimillion dollar liability for the sort of human error which everyone must at some time commit.

The minimum standard, we submit, is that of *Lanza* v. *Drexel & Co.*, 479 F.2d 1277 (2d Cir. 1973). Under *Lanza*, defendants may be held liable only if they knew that unlawful conduct was taking place and ignored it; or if they knew facts from which, through the exercise of reasonable diligence, they could have learned of such violations, and recklessly disregarded those facts. *See also Chris-Craft Industries, Inc.* v. *Piper Aircraft Corp.*, 480 F.2d 341 (2d Cir.), *cert. denied*, 414 U.S. 910 (1973). More recently, in *Ernst & Ernst* v. *Hochfelder*, —— U.S. ——, 96 S. Ct. 1375 (1976), the Supreme Court left open the question whether even reckless disregard of the truth meets the requirements of scienter.

Thus, it is clear that Haupt could not sue Allied for manipulation or improper trading without proof of scienter —either intent to defraud or at a minimum recklessness. If a lesser standard of scienter could be applied in a suit against an exchange, the result would be an absurdity. A broker who could not recover from his customer in the absence of proof of reckless trading could nevertheless recover from the exchange for mere negligence in failing to detect the customer's secret trading.

The evidence with respect to the pre-November 14 period, recited at pages 24-39 above, does not contain a scintilla of evidence that defendants were guilty of knowing or reckless disregard; rather, the record shows that, although the defendants had no reason for alarm, they did make extensive inquiries and were reassured from all available sources—including Haupt—that no condition requiring drastic action existed. Indeed, the District Court gave

plaintiff great leeway in permitting this case to go to the jury, when even the case as to negligence amounted to mere quibbling, twelve years later, with defendants' interpretation of and response to certain facts—principally the statistical "warning signs" constructed after the fact, for the litigation, by plaintiff's expert witnesses. But in any event, defendants' response to the situation that existed before November 14 can by no stretch of the imagination be called reckless disregard.

Still more clearly, the court was right when it determined that plaintiff had failed to produce any evidence of bad faith by defendants with respect to the pre-November 14 period. There is no evidence that the Exchange or any member of its Board of Managers acted with any motive other than to regulate the cottonseed oil futures market fairly and effectively. Plaintiff claims on this appeal, in essence, that the jury should have been allowed to conclude that defendants' alleged negligence was ill-motivated—that defendants deliberately refrained from making the inquiry plaintiff says they should have made, presumably because, for some unknown reason, defendants did not want to prevent Allied and Haupt from destroying through their own greed and folly the cottonseed oil futures market. After seven years of discovery and six weeks in which plaintiff was permitted great latitude in presenting evidence to the jury, the District Court properly declined to let the jury speculate in this manner without any basis in the evidence.

(b) November 14-19

In the period November 14-19, defendants responded to the emergency situation which Haupt and Allied had created. Within four business days, they had taken the drastic step of closing the market entirely and settling contracts at prices fixed by the Exchange. Plaintiff contends not that this step was too drastic—as the shorts protested at the time—but that it should have been taken instantly, when the Exchange learned the size of the Allied position. As explained above (pp. 39-40), this contention was without merit and was not even defended by any of plaintiff's expert witnesses. Still less can it be said that, in not closing the market immediately on November 14, defendants acted in bad faith amounting to fraud.

The test of "bad faith amounting to fraud" was set forth in *Daniel* v. *Board of Trade,* 164 F.2d 815 (7th Cir. 1947), a case similar to this one in pertinent respects and on which plaintiff relies as basic authority for an implied action against an exchange. The plaintiffs in *Daniel* were traders on the Chicago Board of Trade, which like the Exchange was a designated contract market under the Commodity Exchange Act. In response to a sudden change in government price control regulations, the Board of Trade suspended trading in certain commodities and ordered liquidation of contracts at or below the old ceiling prices. Subsequently, the Board reinstated trading at the new higher ceilings, then again terminated the still outstanding contracts.

Short sellers who were injured by the Board's turnabout and the resultant higher closing prices sued the

Board, its clearing corporation, and a number of individuals. The Court of Appeals, noting that the Board of Trade had power under its rules and by-laws to take such action, held that the Board of Trade and its clearing corporation "violated no rights of the plaintiffs in the disposition they made of the plaintiffs' futures contracts, in the absence of an averment of bad faith amounting to fraud." 164 F.2d at 819. As to the directors, governors and officers of the Board of Trade and clearing corporation, the court said that they could be held liable if, and only if, they "did not act in good faith but acted to further their own selfish interests and for their personal gain." 164 F.2d at 820. *See also, Lagorio* v. *Board of Trade,* 529 F.2d 1290 (7th Cir.), *cert. denied,* 44 U.S.L.W. 3738 (June 21, 1976).

Plaintiff did not meet this test. His attempt to show bad faith consists of the baseless assertion that defendants' alleged negligence was ill-motivated. Totally ignoring the defendants' justified wish to avoid a market panic, plaintiff claims that their conduct in keeping Allied's exact position confidential, and in sending out a position call, was a "virtual farce" (Br., p. 50). Because defendants did not act as plaintiff would have wished, plaintiff would have the jury infer that their action had a sinister purpose.

In the case of the Exchange itself, MacDonald, Fashena and Usiskin, no such sinister purpose is even suggested. Plaintiff does claim (Br., p. 51) that Bunge, Continental and Merrill Lynch were engaged in "profiteering," but that claim is totally false and was negated on plaintiff's own case, as the District Court found (see the separate briefs of those defendants).

In short, the District Court correctly concluded that there was no evidence of bad faith by any defendant in either time period. Indeed, we submit that there is no evidence from which a jury could infer even that the defendants were negligent—but mere negligence, demonstrated above, cannot be a basis for liability here. Plaintiff failed, as a matter of law, to prove any conduct that could be a basis for liability, and for that reason his claim under the Commodity Exchange Act should never have been submitted to the jury.

4. Plaintiff Did Not Prove Causation.

Plaintiff's proof failed in yet another vital respect: plaintiff did not prove that Haupt's losses were proximately caused by an act or omission of the Exchange and its directors. On the contrary, all of the evidence, including plaintiff's own admissions, established that Haupt's losses were caused by its heedless over-extension of credit to Allied.

As a broker-member of the Exchange, Haupt was responsible for investigating and satisfying itself as to its customers' financial responsibility. The Exchange had no power to regulate the financial arrangements between broker and customer and, indeed, not until the 1968 amendments to the Commodity Exchange Act were exchanges given the duty of even enforcing minimum financial standards on members. (7 U.S.C. §7a(9)).

Thus, the Exchange did not know that Haupt was extending credit to Allied on warehouse receipts. Stevens had told Berg that Haupt was receiving ample cash margin

from Allied—indeed, in excess of Exchange minimums—and that Allied was meeting all of its obligations (see pp. 35-37 above). The Exchange did not know—again because Stevens lied—that Allied had not even paid Haupt the original margin which Haupt had remitted to the Clearing Association and Chicago brokers (JA 1963a-1964a).

The millions of dollars in cash Haupt was receiving from the Clearing Association in variation margin prior to November 14 were voluntarily turned over to Allied by Haupt, which left itself for its own safety and protection worthless "product margin", despite a vastly escalating position, scaled-up margin requirements, and the prediction of its own commodities man that prices were about to decline because of independent market forces (Barton, JA 1862a-1863a, 1896a).

Even on November 14, when Haupt for the first time received uncertified checks to meet a margin call, Haupt still took no steps to protect itself but only invited greater disaster; the checks were simply tucked under a desk blotter (see p. 21 above). In the face of market declines, Allied's failure to meet further margin calls, and knowledge that Allied was on the verge of bankruptcy, still Haupt did nothing but accumulate the losses which are the subject of this action until November 19, when it was apparently rescued from its own cupidity by the Exchange. Even this proved to have been a false hope when, weeks later, it was discovered that the warehouse receipts Haupt voluntarily accepted in place of cash margin were worthless.

It is, of course, a requirement for recovery in any private damage action that the defendant's dereliction be the

cause of the injury. See *Estate Counseling Service, Inc.* v. *Merrill Lynch, Pierce, Fenner & Smith, Inc.*, 303 F.2d 527, 533 (10th Cir. 1962). As Judge Friendly said in *Ellerman Lines, Ltd.* v. *The President Harding*, 288 F.2d 288, 290 (2d Cir. 1961):

> "Perhaps as good a way to state the rule as any is that a tort defendant is not liable for consequences preventable by action that reason requires the plaintiff to take; per contra if the plaintiff takes such action within the range of reason, the defendant is liable for further damages resulting therefrom. It seems unnecessary to follow McCormick, pp. 127-128, and the Restatement, p. 602, in finding the root of this rule in a policy of discouraging persons from 'wasting their resources both physical or economic'; it is enough that the community's notions of fair compensation to an injured plaintiff do not include wounds which in a practical sense are self-inflicted."

Here, plaintiff ignored this requirement; its own admissions and evidence showed that its losses were caused by its own reckless acts.

B. Count II: Antitrust Claim

No extensive discussion of plaintiff's antitrust claim is necessary. Plaintiff concedes (Br., pp. 45-47) that he must show bad faith to establish his antitrust case and, as we have demonstrated and as the District Court held, plaintiff never produced any evidence of bad faith. This alone justified the District Court in directing a verdict for the defendants on the antitrust claim, as it did at the close of plaintiff's case (JA 1794a).

Moreover, even if there was evidence of bad faith on the part of one or more of the defendants—an indispensable element of plaintiff's antitrust claim—a "contract, combination [or] conspiracy" within the meaning of Section 1 of the Sherman Act, 15 U.S.C. §1, would still be lacking. Plaintiff never even attempted to show any agreement or conspiracy among the defendants, tacit or explicit. No evidence was offered as co-conspirator hearsay or "subject to connection." Rather, plaintiff claimed that each of the defendants, independently, failed properly to carry out his or its regulatory duty. Even if proved, this would not constitute a violation of the antitrust laws.

Plaintiff contends that no proof of an agreement was needed "because, by definition, a commodity exchange is a combination which restrains trade," and is exempt from the antitrust laws only so long as it acts in good faith (Br., pp. 45-47). This argument rests on a misconception. It is true that any exchange, including the New York Produce Exchange, requires an antitrust exemption to carry out regulatory action; but what plaintiff complains of here is defendants' alleged *failure* to act—specifically, an alleged failure to discover the size of the Allied-Haupt position, and an alleged failure to close the cottonseed oil futures market promptly enough. Inaction, unless it is pursuant to some agreement, does not violate the antitrust laws.

Plaintiff did not even attempt to prove an implied agreement for collective inaction. On the contrary, his argument was that each of the defendant directors, for his own reasons, neglected his duties. This is the converse of an antitrust claim. In fact, plaintiff's theory would convert every

action against an exchange for failure to regulate into a treble damage antitrust suit.

The cases on which plaintiff relies in discussing his antitrust claim are all cases in which a plaintiff complained of some regulatory action, such as blacklisting, which would, absent an antitrust exemption, be illegal. No authority supports the assertion of a claim like the present one under the antitrust laws. On the contrary, in the analogous context of suits against private regulatory bodies accused of bad faith, the courts have held that there must be a showing of "sufficient agreement to constitute a 'contract, combination . . . or conspiracy.'" *McCreery Angus Farms* v. *American Angus Ass'n*, 379 F. Supp. 1008, 1017 (S.D. Ill.), *aff'd mem.*, 506 F.2d 1404 (1974); *Blalock* v. *Ladies' Professional Golf Ass'n*, 359 F. Supp. 1260, 1263 (N.D. Ga. 1973); *Denver Rockets* v. *All-Pro Management, Inc.*, 325 F. Supp. 1049, 1062 (C.D. Cal. 1971); *see also Cowen* v. *New York Stock Exchange*, 256 F. Supp. 462, 467 (N.D.N.Y. 1966); *Kline* v. *Coldwell, Banker & Co.*, 508 F.2d 226 (9th Cir. 1974), *cert. denied*, 421 U.S. 963 (1975).

Finally, even if the essential elements of an antitrust claim were present, Haupt's own misconduct would bar recovery. Plaintiff's reliance on *Perma Life Mufflers, Inc.* v. *International Parts Corp.*, 392 U.S. 134 (1968), as holding the contrary is misplaced. This Court has made clear that *Perma Life* is in fact authority for upholding the defense of *in pari delicto* where the plaintiff's fault equals or exceeds the defendant's. In *Bernstein* v. *Universal Pictures, Inc.*, 517 F.2d 976 (2d Cir. 1975), the court rejected a defense of estoppel in the antitrust cases before it, but said:

"We do not hold today that under no circumstances will estoppel be a sufficient defense to an antitrust action. *As a majority of the court recognized in Perma Life, a plaintiff may properly be denied antitrust relief when his culpability is equal to that of the defendant.*" (Emphasis added)

Id. at 982; *accord, Columbia Nitrogen Corp.* v. *Royster Co.*, 451 F.2d 3, 15-16 (4th Cir. 1971); *South-East Coal Co.* v. *Consolidation Coal Co.*, 434 F.2d 767, 784 (6th Cir. 1970), *cert. denied*, 402 U.S. 983 (1971); *Premier Electrical Const. Co.* v. *Miller-Davis Co.*, 422 F.2d 1132, 1138 (7th Cir.), *cert. denied*, 400 U.S. 828 (1970).

The antitrust claim was properly dismissed by the District Court.

POINT II

There was no error in the court's charge of which plaintiff can complain.

Plaintiff contends that the District Court's charge was too favorable to the defendants in several respects. Brief discussion of plaintiff's specific criticisms demonstrates that each of them is without merit.

A. The Jury Was Properly Allowed to Consider Haupt's Misconduct.

Plaintiff says that the jury should have been instructed "to ignore" what plaintiff calls "Haupt's alleged contributory negligence" (Br., p. 84). As demonstrated above, Haupt's conduct was far worse than "negligence"—recklessness is the mildest possible word that could be used

—and there is no basis in law for ignoring it. To ignore Haupt's misconduct would not, as plaintiff says, ensure "stringent enforcement" of the Commodity Exchange Act (Br., p. 86), but would vitiate such enforcement by absolving brokers like Haupt from their vital responsibility in the regulatory scheme, and "turn the Act on its head." *New York Stock Exchange, Inc.* v. *Sloan,* 394 F. Supp. 1303, 1315 (S.D.N.Y. 1975).

By stressing his contention that Haupt's conduct should have been ignored, plaintiff implicitly concedes that any fact finder who considered Haupt's conduct would have to find for defendants in this case.

B. Plaintiff's Proposed Charge on Defendants' Recklessness Was Not Requested and Would Not Have Been Proper.

Plaintiff argues, in the alternative, that the court should have instructed the jury "that if they found defendants to have acted in reckless disregard of their duties, then they should ignore the allegations of Haupt's contributory negligence" (Br., p. 88). No such charge was requested; plaintiff elected to stand squarely on his contention that Haupt's conduct should be removed, under all circumstances, from the jury's consideration. The case cannot be reversed for failure to give a charge which was not requested. *Cohen* v. *Franchard Corp.,* 478 F.2d 115, 122 (2d Cir.), *cert. denied,* 414 U.S. 857 (1973).

In any event, the charge which plaintiff now proposes is not justified. There was no proof, as we have demonstrated, from which the jury could find that defendants

acted recklessly. Moreover, assuming, contrary to fact, that defendants were reckless, it is incontestable that Haupt was more so. If the risks inherent in Haupt's position were so obvious as to make the Exchange action reckless, they were even more obvious to Haupt.

The key point is that Haupt's culpability, beyond dispute, exceeded that of which defendants are accused. This gives defendants a complete defense to the action, even if their conduct has been negligent, reckless or worse. In *Kuehnert* v. *Texstar Corp.*, 412 F.2d 700 (5th Cir. 1969), defendant was guilty of *intentional* fraud. Plaintiff's own misconduct was nevertheless held to bar recovery; the court said that his "intention differed from [the defendant's], but it was no more commendable." *Id.* at 704.

C. No Further Charge Was Necessary on the Scope of Stevens' Employment.

Plaintiff claims that the District Court should have charged the jury "with respect to whether the conduct of Jack Stevens was attributable" to Haupt (Br., pp. 88-90). The court in fact instructed the jury to consider the actions of Haupt or its "officers or employees, acting within the scope of their employment." (JA 2116). Plaintiff accepted this charge and did not request a more detailed definition,* perhaps because it is perfectly obvious, from the facts summarized at pages 15-16 above, that Stevens' conduct *was* the conduct of Haupt.

* Plaintiff did request that the argument that Stevens' actions were not attributable to Haupt be mentioned in the charge as one of plaintiff's contentions (JA 2119a-2120a). This contention was frivolous, for the reasons stated in the text, and the court properly rejected plaintiff's request. *Quercia* v. *United States*, 289 U.S. 466, 470 (1933).

Plaintiff argues that Stevens' acts were unauthorized because "he acted illegally and certainly contrary to Haupt's best interests" (Br., p. 89). But this misses the point. Stevens concededly had full charge of Haupt's commodity department, and third parties, including the defendants, were entitled to rely upon his words and conduct with respect to Haupt's commodity business as being the words and conduct of Haupt. "[C]onduct may be within the scope of employment even if it is unauthorized, if it is sufficiently similar to authorized conduct." *Lewis* v. *Walston & Co.*, 487 F.2d 617, 624 (5th Cir. 1973); *see also* Restatement (2d), Agency §229 (1968); *Fey* v. *Walston & Co.*, 493 F.2d 1036 (7th Cir. 1974).

An employer cannot escape responsibility for his employee's actions merely by claiming that he did not authorize an illegal or tortious action. Restatement (2d), Agency §§230, 231 (1958). The owner of a bus company could not escape responsibility for a bus driver's reckless driving merely by arguing that he had never authorized the driver to exceed the speed limit. And certainly, the bus company would have no claim against a traffic policeman who allegedly failed to stop the speeding bus before it crashed. The whole idea of pretending that Haupt is not responsible for Stevens' acts is frivolous.

D. The Charge on the November 14-19 Standard of Conduct Was Too Favorable to Plaintiff.

Plaintiff complains of the District Court's charge that, with respect to the November 14 to 19 period, an "abuse of discretion" standard was applicable to defendants' conduct. The court charged, in brief, that a defendant could

be held liable with respect to this time period only if he or it "failed reasonably to carry out his or its duties and abused his discretion in regulating the market"; the court explained that "a director has broad discretion in making business judgments. . . . The standard here is not what the defendant might have done or could have done or even should have done, but whether the acts of the defendant can be said to have been so patently unreasonable as to constitute an abuse of discretion." (JA 2113a-2114a).

Plaintiff's sole ground for attacking this charge is that, according to plaintiff, defendants were not entitled to the benefit of the "emergency" doctrine because the emergency was of their own making (Br., pp. 91-92). This argument has several flaws: (1) there was, as demonstrated above, no evidence to support the contention that the defendants were at fault in creating the emergency; (2) if the jury had found, contrary to the evidence, that the defendants were at fault in the pre-November 14 period, they were instructed by the court to return a verdict for plaintiff (subject to a determination of Haupt's conduct); and (3) the abuse of discretion standard applies to all actions by a board of directors exercising business judgment, not just to actions taken in an emergency.

Indeed, the authority most closely in point holds, as discussed at pages 64-66 above, that in a situation like that existing in the November 14 to 19 period, liability can be imposed only for "bad faith amounting to fraud"—a proposition consistent with *Ernst & Ernst* v. *Hochfelder*, —— U.S. ——, 96 S. Ct. 1375 (1976). Other authorities, even before *Hochfelder*, make clear that the most stringent standard which could possibly be applied to defendants' conduct is the "abuse of discretion" standard set forth by

the District Court.* *International Industries, Inc.* v. *American Stock Exchange,* 452 F.2d 935, 940 (5th Cir. 1971), *cert. denied,* 409 U.S. 842 (1972) (an exchange must have "broad latitude"); *J. R. Williston & Beane, Inc.* v. *Haack,* 387 F. Supp. 173, 181 (S.D.N.Y. 1974); *Financial Industrial Fund, Inc.* v. *McDonnell Douglas Corp.,* 474 F.2d 514, 518 (10th Cir.), *cert. denied,* 414 U.S. 874 (1973).

Plaintiff has no genuine ground to complain of the charge, which was unduly favorable to him in not requiring scienter in the *Hochfelder* sense.

E. An Instruction to Ignore the Evidence of CEA Inaction Would Have Been Erroneous.

Plaintiff claims that the District Court erred in failing "to instruct the jury to ignore the evidence of CEA inaction" in 1963. This contention is almost incomprehensible. The court did not affirmatively instruct the jury that it should consider CEA inaction; it rejected defendants' requests for such instructions (Defendants' request no. 63, JA 193a). Indeed, the charge makes no reference to the CEA except in summarizing the parties' contentions. The District Court charged that the Exchange had "initial responsibility" for maintaining an orderly market (JA 2112a).

Defendants have never contended that inaction by the CEA absolved the defendants of their regulatory duties.

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* The *Daniel* case, discussed at pages 64-66 above, refers to "exercise of discretion" by a board of directors, as well as the need for showing "bad faith." 164 F.2d at 819. Thus the two standards are not inconsistent. We believe that the District Court erred in plaintiff's favor in applying only the "abuse of discretion" and not also the "bad faith" test.

We do contend—and it is self-evident—that defendants were entitled to draw some reassurance, in 1963, from the fact that the CEA, which had information and resources the Exchange did not have, apparently saw no need for regulatory action. Indeed, the CEA responded to specific inquiries, both from Berg and Anderson, by telling the Exchange in substance that there was nothing to be alarmed about. (See pages 34, 37 above.)

It cannot be disputed that the CEA's inaction and its reassurances to the Exchange, like all other facts known to defendants at the pertinent times, were *relevant* to the question of how well the defendants discharged their regulatory duties. Evidence of these events was admitted, largely without objection. We cannot imagine why the jury should have been instructed to ignore this evidence, and clearly such an instruction would have been error.

POINT III

There was no error of which plaintiff can complain in the rulings on evidence.

A. Evidence Offered by Plaintiff

As noted above (pp. 49-50), the District Court allowed plaintiff very substantial leeway in its rulings on evidence; much potentially prejudicial material, of dubious relevance, was admitted. Plaintiff is not content with this degree of indulgence, however, and complains of several occasions during the trial in which the District Court sustained objections to evidence proffered by plaintiff. All of the rulings about which plaintiff complains were correct.*

* Rulings applicable only to particular defendants will be discussed, to the extent necessary, in the separate briefs of those defendants.

1. Evidence Relating to Soybean Oil

Plaintiff attacks the District Court's exclusion of evidence as to transactions in soybean oil on the Chicago Board of Trade. But this case, as the court repeatedly had to remind plaintiff, was concerned with the defendants' regulation of trading in cottonseed oil futures on the New York Produce Exchange. What was happening in a different commodity on a different Exchange was simply irrelevant to what the defendants saw or could have seen on the New York Produce Exchange and whether they properly carried out their regulatory duties there. *See* JA 1643a-1646a, 1926a, 1725a-1726a; *see also, Olsen* v. *Realty Hotel Corp.*, 210 F.2d 785, 786 (2d Cir. 1954). Plaintiff argues (Br., pp. 53-54) that any profits made on soybean oil transactions would be probative of defendants' alleged bad faith in regulating the cottonseed oil market; but plaintiff never even tried to prove that the way in which the defendants regulated the New York Produce Exchange would affect prices on the Chicago Board of Trade. Exploration of soybean oil transactions was not only irrelevant, but would have been time-wasting and confusing to the jury. The District Court properly exercised its broad discretion to exclude such evidence.

2. The Testimony of Robert Raclin

Robert Raclin was one of five "expert" witnesses called by plaintiff; he was called on plaintiff's rebuttal case and, after he failed to qualify, plaintiff brought in another rebuttal expert, Professor Paul Farris, to replace him. Raclin's proffered testimony, as described by counsel at trial (JA 1940a-1953a), would have been merely cumulative of

the other experts, and thus any error in excluding his testimony was harmless. *Joseph T. Ryerson & Son, Inc.* v. *H. A. Crane & Brother, Inc.*, 417 F.2d 1263 (3d Cir. 1969); *Williams* v. *Steuart Motor Co.*, 494 F.2d 1074 (D.C. Cir. 1974).

In any event, the District Court was correct in ruling that plaintiff had failed to qualify Raclin as an expert witness, for Raclin did not show sufficient knowledge of a relevant custom and usage. He testified that he was a member of the Board of only one regulated commodities exchange—the Chicago Board of Trade (JA 1930a); that commodities exchanges are not identical (JA 1929a); that the committees of various exchanges vary in the way they operate from exchange to exchange (JA 1930a-1931a); and that he was not familiar with the operations of the Produce Exchange. For example, Raclin did not know in 1965 whether unregistered American Express receipts could be tendered on the Produce Exchange (JA 1938a). Thus Raclin's own testimony does not support the suggestion, made in plaintiff's brief, that the difference between commodities exchanges are "of no moment" (Br., p. 69).

3. The Testimony of Perry Moore

Plaintiff's sole purpose in seeking to call Perry Moore as a witness was to provide a foundation for the introduction into evidence of two letters (PX 25 id., JA 149e-150e; PX 26 id., JA 151e) which Moore had written in April and May, 1963 when he was a director of the Clearing Association, and not of the Produce Exchange (JA 424a-426a). These letters, which express some concern about the activities of an unidentified brokerage firm, several months be-

fore the collapse of Allied, were sent to the Clearing Association, not to the Produce Exchange. No evidence was offered that any defendant ever knew that the letters were sent, or that any defendant knew Moore was concerned about the market (JA 428a). Plaintiff made no offer to qualify Moore as an expert; moreover, Moore's letters were based on information not available to any defendant. Members of the Clearing Association board, but not the Produce Exchange board, knew the net positions of clearing members, and it was the net position of "Firm 'N'" that prompted Moore to write his letters.

The District Court rightly concluded that opinions based on facts unkown to the defendants, and never communicated to the defendants were not admissible in evidence.

4. *Other Excluded Evidence*

Under the heading "other limitations and exclusions" (Br., pp. 64-67), plaintiff complains of rulings which upheld defendants' objections to some of his more egregiously misleading charts and summaries of data relating to the so-called "warning signs." The most basic objection to these charts and summaries is that they would have been highly misleading to the jury as to what defendants could or should have seen in 1963. They either oversimplified complex and voluminous material concerning the cottonseed oil market (*see, e.g.*, PX 122a id., JA 509e, JA 290a-296a, 318a-320a; PX 123a id., JA 513e, JA 297a-298a), or they "illustrate[d] graphically," as plaintiff puts it (Br., p. 64), information which defendants would not have seen in 1963 because the information was kept confidential or because it would not normally have been received by the defendants and there was no reason during the relevant time period for

them to ask for it (*see, e.g.*, PX 130 id., JA 529e; PX 131 id., JA 531e, JA 1626a-1628a, 1630a-1632a; PX 124a id., JA 517e, JA 304a-307a; PX 125a id., JA 521e, JA 307a-312a, 321a-322a; PX 126a id., JA 525e, JA 299a-302a). Plaintiff did not even offer all of the exhibits about which he now complains into evidence (A 362a; PX 131a id., JA 533e and 133a id., JA 537e were not offered).

The court's rulings were made in areas where the trial court has broad discretion to avoid jury confusion and prejudice, and they were entirely proper.

In sum, the limitations which the District Court placed on plaintiff's proof were all appropriate. In this area as in others, the court's rulings were if anything too favorable to the plaintiff.

B. The CEA Investigative Report

Defendants' Exhibit 1A was an official CEA document, identified as such, and entitled "Report of Investigation of the Operations of Allied Crude Vegetable Oil Refining Corporation in Cottonseed Oil Futures and Soybean Oil Futures July 1, 1963-November 22, 1963." It reviews in detail the facts available to the CEA concerning Allied's activities—the positions held by Allied and other traders, the production and supply of edible fats and oils, other economic factors affecting the prices of cottonseed oil, the relationship between cash and futures prices of cottonseed oil, trends in the futures prices of cottonseed oil and the relationship between the prices of cottonseed oil and other oils.

After setting forth and interpreting these facts in detail, the CEA concluded that there was no actual or threatened corner or squeeze in the cottonseed oil market in 1963; that cottonseed oil prices were not artificial but were justified by economic factors; and that it was unreasonable to assume that DeAngelis, an experienced trader, intended a manipulation in a situation where—since supplies of oil were ample—a manipulation would be most unlikely to succeed.

In response to plaintiff's attempt to show, through expert witnesses, that the danger of a corner or squeeze did exist and that there were artificial prices and a successful manipulation, defendants offered the CEA report into evidence. Plaintiff was given ample opportunity to attack this report through expert witnesses called in rebuttal, but he nevertheless claims on this appeal that the admission of the report into evidence was error.

Plaintiff's attacks on the District Court's ruling are foreclosed by Rule 803(8)(C) of the Federal Rules of Evidence, which is squarely applicable to this document. The rule provides that documents in the following category may be admitted as an exception to the hearsay rule:

> (8) *Public records and reports.* Records, reports, statements, or data compilations, in any form, of public offices or agencies, setting forth—
>
> (C) in civil actions and proceedings and against the Government in criminal cases, factual findings resulting from an investigation made pursuant to authority granted by law, unless the sources of information or other circumstances indicate lack of trustworthiness.

Despite this provision, plaintiff's principal objection to the report is that it is hearsay. Plaintiff protests that he "was confronted with a written opinion which he could subject to neither *voir dire* nor cross-examination" (Br., p. 69). He contends that the District Court should have applied the hearsay rule through the back door of Rule 403, which provides that relevant evidence "*may* be excluded if its probative value is substantially outweighed by the danger of unfair prejudice, confusion of the issues or misleading the jury. . . ." (Emphasis added.)

Plaintiff's longing for "the sunshine of *voir dire* and cross-examination" is hypocritical. Plaintiff himself obtained the CEA report from the CEA well before trial, under the Freedom of Information Act; he never sought to depose its author. Alex C. Caldwell, the CEA Administrator under whose supervision the report was prepared, appeared on plaintiff's trial witness list but was never called. In any event, assuming that the District Court had discretion under Rule 403 to exclude the report, it also had discretion to admit it. The value of a government report prepared shortly after the time in question, by an agency with unique access to the pertinent sources of information and unique expertise in evaluating those sources, suffices to demonstrate that the District Court did not abuse its discretion in overruling plaintiff's objection.

Indeed, plaintiff's argument against the admission of the CEA report runs counter to the Supreme Court decisions in *Chicago Mercantile Exchange* v. *Deaktor*, 414 U.S. 113 (1973), and *Ricci* v. *Chicago Mercantile Exchange*, 409 U.S. 289 (1973). In those cases, the Supreme Court directed

that actions against commodities exchanges be stayed pending examination by the CEA of the exchanges' conduct since a determination by the CEA would be "a material aid" in resolving the lawsuits. 409 U.S. at 305. It would make a mockery of the Supreme Court's rationale to hold that where the CEA has conducted an investigation its analysis should be withheld from the jury.

Plaintiff's efforts to find some more solid legal basis for objecting to the CEA investigative report are in vain. His brief raises objections based on the personal knowledge rule, the opinion rule, Rule 1006 of the Federal Rules of Evidence, and the "trustworthiness" provisions of Rule 803(8)(C). All the objections are unsound.*

1. The Personal Knowledge Rule

Plaintiff is wrong in saying that government reports are admissible under Rule 803(8)(C) only where the author of the report demonstrably had personal knowledge of the facts stated. Prior to the enactment of the new, liberalized Federal Rules of Evidence, the cases generally considered the admissibility of government reports in the context of the old federal business records statute, 28 U.S.C. §1732, which expressly provided that lack of personal knowledge

* There is no merit to plaintiff's suggestion (Br., fn., pp. 75-76) that the report was not sufficiently identified or authenticated. The Federal Rules of Evidence require only a showing that the document is what it purports to be. Rule 901(a). In the case of a public record or report, the showing may be made by evidence that the office from which it was taken was the legal custodian of the record or report. Federal Rules of Evidence, Rule 901(b(7); 5 Weinstein, *Evidence* ¶901(b)(7) [01] at 901-92, 901-95 (1975). The CEA report was authenticated by a certificate from the acting director of the Bureau of Market Surveillance of the Commodity Futures Trading Commission, the federal agency to which all CEA records were transferred by statute. See Rule 902, Federal Rules of Evidence.

by the maker of the report would not affect its admissibility, but only its weight. Thus, contrary to the statement in plaintiff's brief (p. 77), government reports were not automatically excluded, even before the enactment of the federal rules, merely because they contained statements of which their author did not have firsthand knowledge. *See, e.g., Smith* v. *Universal Services, Inc.*, 454 F.2d 154, 158 & n. 2 (5th Cir. 1972); *White* v. *Zutell*, 263 F.2d 613, 615 (2d Cir. 1959); *Pekelis* v. *Transcontinental & Western Air*, 187 F.2d 122, 130-31 (2d Cir.), *cert. denied*, 341 U.S. 951 (1951); *Moran* v. *Pittsburgh-Des Moines Steel Co.*, 183 F.2d 467, 473 (3d Cir. 1950).

The same approach continues under the Federal Rules of Evidence. While the introduction to the Advisory Committee's Note on Rule 803 indicates that the requirement of firsthand knowledge generally is not affected by the hearsay exception, the Advisory Committee's discussion of particular sections of Rule 803—including the new business records exception [Rule 803(6)] and the official reports exception [Rule 803(8)]—indicates that the general principle is overridden in appropriate circumstances, where the circumstantial guarantee of trustworthiness—*i.e.*, the justification for the hearsay exception—is based upon a factor other than personal observation.

As to Rule 803(8), the justification for the exception, as described in the Advisory Committee's Note, is "the assumption that a public official will perform his duty properly and the unlikelihood that he will remember details independently of the record." The "duty" of the official in the Rule 803(8)(C) situation is not to report accurately

upon activities he personally performed or facts he personally observed (compare Rule 803(8)(A) and (B)), but to make an investigation pursuant to authority granted by law. As Wigmore recognized before the Federal Rules of Evidence were enacted, the personal knowledge requirement is irrelevant to the admissibility of such an investigative report:

> "[T]here may be cases in which *the officer's duty clearly does involve his ascertainment of facts occurring out of his presence and requiring his resort to sources of information other than his own senses of observation.* . . . When such a duty clearly exists, *the general doctrine* above, *that a witness should have personal knowledge, need not stand in the way,* for (as already noted) it has its conceded limitations; and where the officer is vested with a duty to ascertain for himself by proper investigation, this duty should be sufficient to override the general principle." (Emphasis added.)

5 Wigmore, *Evidence,* §1635 at 639 (3d ed. 1974); *see also,* 4 Weinstein, *Evidence, supra,* §803(8)[03] at 803-181; McCormick, *Can the Courts Make Wider Use of Reports of Official Investigations?,* 42 Iowa L. Rev. 363 (1957).

Yung Jin Teung v. *Dulles,* 229 F.2d 244 (2d Cir. 1956), a pre-Federal Rules case cited by plaintiff for the proposition that lack of personal knowledge bars receiving an official investigative report into evidence, is not pertinent here. *In Yung Jin Teung,* the report was not prepared pursuant to a statutory duty to investigate. To the contrary, the court concluded that the report was prepared by the defendant, the Secretary of State, for the purposes of the

litigation. *Id.* at 247. Here, the CEA's report was prepared pursuant to a duty to which the Supreme Court gave precedence in *Ricci* and *Deaktor*.

The personal knowledge rule is inapplicable to the CEA report.

2. *The Opinion Rule*

Plaintiff claims that the CEA report should have been excluded "to the extent that it contains expert opinions and conclusions" (Br., p. 76) because no independent evidence was presented of the author's expertise. Most of the report is fact, not opinion; in any event, the admission of opinions and conclusions as part of the investigative report was proper.

A government investigative report will normally contain expert conclusions. In rendering such reports admissible, Rule 803(8)(C) contemplates that the conclusions will come in also. This is recognized in the Advisory Committee's Note; after cataloguing various cases and statutes admitting investigative reports, the Note concludes that the Rule "assumes admissibility in the first instance," with an opportunity for the trial court in its discretion to exclude a particular report which is insufficiently trustworthy. *See SEC* v. *General Refractories,* 400 F. Supp. 1248, 1255-56 (D.D.C. 1975). Among the statutes referred to as exemplifying the sort of report made admissible by Rule 803(8)(C) are those providing for the admission into evidence of evaluative reports of government

agencies—including evaluative reports by the Secretary of Agriculture. *See, e.g.,* 7 U.S.C. §§79, 210(f), 292.*

In the analogous areas of reports of accident investigations and medical diagnoses, this Court regularly has held that opinions and conclusions are properly admitted when within the investigator's area of competency. *See Caldecott* v. *Long Island Lighting Co.,* 417 F.2d 994, 996 (2d Cir. 1969); *Taylor* v. *Baltimore & Ohio R.R. Co.,* 344 F.2d 281, 285-86 (2d Cir. 1965), *cert. denied,* 382 U.S. 831 (1965); *Pekelis* v. *Transcontinental & Western Air,* 187 F.2d 122 (2d Cir.), *cert. denied,* 341 U.S. 951 (1951).

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* The legislative history of Rule 803, read as a whole, does not contradict the implication of the Advisory Committee's Notes that the conclusions on the investigative reports are admissible. The House Judiciary Committee, without any further discussion or support, did state that the phrase "factual findings" used in Rule 803(8)(C) should be strictly construed to exclude opinions contained in public reports. Report on Federal Rules of Evidence, Committee on the Judiciary, House of Representatives, 93rd Congress, 1st Session, No. 93-650, p. 14 (1973). Thereafter, however, the Senate Judiciary Committee took "strong exception to this limited understanding of the application of the rule," stating:

> "We do not think it reflects an understanding of the intended operation of the rule as explained in the Advisory Committee's Notes to this subsection. The Advisory Committee's Notes on subsection (c) of this subdivision point out that various kinds of evaluative reports are now admissible under Federal statutes . . . . These statutory exceptions to the hearsay rule are preserved. Rule 802. The willingness of Congress to recognize these and other such evaluative reports provides a helpful guide in determining the kind of reports which are intended to be admissible under this rule. We think the restrictive interpretation of the House overlooks the fact that while the Advisory Committee assumes admissibility in the first instance of evaluative reports, they are not admissible if, as the Rules states, 'the sources of information or other circumstances indicate lack of trustworthiness."

Report of the Committee on the Judiciary, Senate, 93rd Congress, 2d Session, No. 93-1277, p. 18 (1974).

The subsequent Conference Report did not refer to this question. Congressional Record—House, December 14, 1974, H-11931-32; *see* 4 Weinstein, *Evidence, supra,* at 803-230.

The expertise of the CEA with respect to the subject matter of its report—trading in the cottonseed oil futures market during 1963—cannot seriously be questioned. The facts relied upon by the CEA in its investigation are precisely the kind of data upon which an expert in this area would rely. There was no basis for excising the report's conclusions.

3. Rule 1006

Plaintiff contends (Br., pp. 79-80) that Rule 1006 of the Federal Rules of Evidence required defendants to make available all the raw data underlying the CEA report before it could be introduced into evidence. This contention is absurd; if accepted, it would nullify Rule 803(8)(C).

Rule 1006 provides a convenient means of putting before a trier of fact "the contents of voluminous writings, recordings or figures which cannot conveniently be examined in court"; instead of introducing the voluminous exhibits, a party may introduce summaries, and make the underlying documents available to the other parties. This Rule was clearly intended to promote the convenience of the parties and the court; it was not intended to limit the operation of Rule 803(8)(C).

Many if not most investigative reports of government agencies offered pursuant to Rule 803(8)(C) will contain charts, summaries or calculations summarizing the data gathered by the government agency. The remedy of a party who is dissatisfied with this summary is to seek from the government agency the raw data itself. In this case, plaintiff obtained extensive pretrial discovery from the CEA. *Freeman* v. *Seligson,* 405 F.2d 1326 (D.C. Cir. 1968).

4. *The Trustworthiness of the Report*

Finally, plaintiff argues that, in the language of Rule 803(8)(C), "the sources of information or other circumstances indicate lack of trustworthiness" of the CEA report. The contrary is true. The trustworthiness of the document is apparent from the report itself and from the affidavit of the Administrator of the CEA, Alex C. Caldwell, which was considered by the District Court in ruling on admissibility of the document (DX 107 id., JA 1113e-1118e).*

The CEA's "sources of information" included confidential daily reports filed by Allied and other reporting traders and commodities futures brokers pursuant to the requirement of the Commodity Exchange Act. The reporters were subject to penalties for any misrepresentation in those reports. 7 U.S.C. §§6, 6f, 6g, 6i, 7-7b, 13 (1964 and 1976 Supp.); 17 C.F.R. Part 15-21; 18 U.S.C. §1001. The CEA had available, in addition to these reports, the reports of its observer on the Exchange trading floor, and other information obtainable from trade publications and elsewhere, relevant to cottonseed oil futures trading. The CEA could analyze this data with the aid of its trained staff of accountants and economists. Its report was prepared shortly after the events in suit, not by a party to this litigation and not in contemplation of any lawsuit. It was prepared, as appears from a memorandum annexed to the report, under the personal supervision of the CEA Administrator. The circumstances did not indicate "lack of trustworthiness"; they indicated the exact opposite.

* Caldwell's affidavit, though not itself admitted into evidence, could properly be considered on the issue of whether the report was admissible under Rule 104(a), Federal Rules of Evidence. See the Advisory Committee's Note accompanying Rule 104(a).

The CEA investigative report was properly admitted into evidence. The report provided the very "aid" to the trier of fact which the Supreme Court in *Ricci* and *Deaktor* sought to promote.

Conclusion

Plaintiff has had more than fair opportunity to establish his claims. The judgment entered on the jury verdict after seven weeks of trial should be affirmed.

Dated: New York, New York
June 11, 1976

Respectfully submitted,

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Affidavit of Service by Mail

In re:

Miller v New York Produce Exchange

State of New York
County of New York, ss.:

Michael Lane,

being duly sworn, deposes and says, that he is over 18 years of age. That on ...., 197...., he served 2 copies of the within Brief in the above named matter on the following counsel by enclosing said two copies in a securely sealed postpaid wrapper addressed as follows:

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